Scottish Law Commission

promoting law reform

(SCOT LAW COM No 249)

Report on Moveable Transactions Volume 1: Assignation of Claims

report

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The Scottish Law Commission was set up by section 2 of the Law Commissions Act 1965 (as amended) for the purpose of promoting the reform of the law of Scotland. The Commissioners are:

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SCOTTISH LAW COMMISSION

Item No 1 of our Ninth Programme of Law Reform

Report on Moveable Transactions

To: Michael Matheson MSP, Cabinet Secretary for Justice

We have the honour to submit to the Scottish Ministers our Report on Moveable Transactions

(Signed) PAUL B CULLEN, *Chairman*
C S DRUMMOND
D E L JOHNSTON
HECTOR L MACQUEEN
ANDREW J M STEVEN

Malcolm McMillan, *Chief Executive*
29 November 2017

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Glossary and abbreviations

ABFA. The Asset Based Finance Association (part of UK Finance since July 2017).

Accessoriness principle. The principle that a security right has no independent existence, but is merely accessory to, or parasitical upon, another right, namely the obligation whose performance it secures. An Arizona court put it thus: "The note [= personal obligation] is the cow and the mortgage the tail. The cow can survive without the tail, but the tail cannot survive without the cow" (*Best Fertilizers of Arizona Inc v Burns*, 117 Ariz 178, 571 P 2d 675 (App 1977)). The secured obligation does not have to be an obligation owed by the provider of the security: one person can provide a security for another's debt.

Account debtor or account party. If X owes money to Y, and Y assigns the claim to Z, X is the account debtor or account party. The term is used rather than simply "debtor" because in some cases Y is also a debtor (to Z). Also called the *debitor cessus*.

Accounts. Also called accounts receivable, or receivables, or book debts. See "receivables".

Accretion of title. If X purportedly transfers a right to Y, but in fact X does not have that right, Y does not acquire it: *nemo plus juris ad alium transferre potest quam ipse haberet*. But if X thereafter acquires the right, then that right passes instantly and automatically to Y. This is called accretion of title.

After-acquired property/assets. In general, security rights can affect only assets held by the provider at the time the security right is created. But some security rights can also affect after-acquired assets, ie assets acquired at a later date. Under current law, three types of security right have this power, the most important being the floating charge. (The others are the agricultural charge, and the landlord's hypothec.) After-acquired assets are also known as future assets.

Agricultural charge. A security under the Agricultural Credits (Scotland) Act 1929. It is a non-possessory security over the inventory (including after-acquired inventory) of certain agricultural co-operative associations.

Aircraft mortgage. A non-possessory security over an aeroplane, created by registration. See the Mortgaging of Aircraft Order 1972 (SI 1972/1268).

Alienation. To alienate is to transfer to another person.

Anti-assignation clause. A clause in a contract forbidding the assignation of rights arising under the contract. Also called a non-assignment clause or a *pactum de non cedendo*.

Anticipatory assignation. The assignation of a right that the cedent does not yet have, in the expectation that it will be acquired. Also called *cessio in anticipando.*

Appropriation. A remedy of a secured creditor whereby ownership of encumbered property is acquired and the value acquired is applied towards satisfaction of the secured obligation. If the value is greater than that obligation then the excess must be returned to the provider.

Archive record. The parts of the Register of Assignations and Register of Statutory Pledges in which entries are archived.

Arrestment. See "diligence."

Assignation or assignment. The transfer of incorporeal property from the assignor (also called the cedent), to the assignee (also, though rarely, called the cessionary). "Assignation" is the term generally used in Scotland, "assignment" in England and other common law systems. In many countries it is called "cession". Assignation may be (a) "outright" or "absolute" or (b) in security. Where there is an assignation in security the property is being used as collateral for a debt owed to the assignee. Absolute/outright assignation is sometimes identified with assignation by reason of sale, but this is not accurate, because it may happen for other reasons as well, such as exchange or even donation. Assignation (whether outright or in security) involves three stages, though the first two may be merged in practice: (i) contract to transfer; (ii) act of transfer; and (iii) intimation to the account debtor. The claim is transferred, ie passes from the assignor's patrimony to the assignee's, only at the third stage.

Assignations record. The principal part of the Register of Assignations.

***Assignatus utitur jure auctoris*.** (Literally, an assignee exercises the right of the author. "Author" here means assignor.) The assignee obtains no better right than the assignor had, so that the account debtor can plead against the assignee any defences that could have been pled against the assignor. Example: Seller sells goods to Buyer on credit, and then assigns the invoice to Financier. If the goods are defective, Buyer can plead that fact as against Financier's claim for payment, just as it could have been pled against Seller's claim for payment. This is so even if Financier was unaware of the problem. Thus assignation does not impair the account party's rights. Financier has no active liability for the Seller's obligations (for example to pay damages). Negotiable instruments are a partial exception to the *assignatus utitur* principle.

Assignee. A person in whose favour an assignation is granted.

Assignor. A person who assigns. See also "Cedent".

Attachment. This term has three different meanings. (i) In Scotland, a synonym for crystallisation of a floating charge. (ii) Also in Scotland, the seizing of an asset by an unpaid creditor, an aspect of the law of diligence. (See "diligence".) (iii) Under UCC–9 and the PPSAs a security interest is said to attach when it becomes effective as between debtor and creditor. An attached security that is not perfected is not normally effective against third parties, though this principle is subject to some exceptions.

Australian Statutory Review 2015. *Review of the Personal Property Securities Act 2009: Final Report* (2015) available at

https://www.ag.gov.au/consultations/pages/StatutoryreviewofthePersonalPropertySecuritiesAct2009.aspx. The review, by Bruce Whittaker, considered how well the legislation was operating two years after it came into force.

Automated register. A register that is operated by a computer system with ordinarily no human involvement.

Bill of exchange. A type of negotiable instrument. In the USA called a "draft".

Bill of lading. A document issued by a shipping company when goods are shipped. The goods are later released to the holder, at the time of presentation of the bill of lading. A bill of lading thus constitutes indirect possession of the goods. See also "trust receipt financing".

Bill of sale. A concept of English law. It is not easy to pin down, but (notwithstanding the name) most bills of sale are non-possessory chattel mortgages. There is no equivalent in Scotland. Regulated by the Bills of Sale Act 1878, the Bills of Sale Act (1878) Amendment Act 1882, the Bills of Sale Act 1890 and the Bills of Sale Act 1891. In certain types of case, transactions other than securities over chattels are registrable. For example, the Insolvency Act 1986 section 344 requires the registration of certain assignments. "The masters of the … Queen's Bench Division … shall be the registrar …" (Bills of Sale Act 1878). The Bills of Sale (1878) Amendment Act 1882 section 11 provides for a local registration system, but such registrations do not oust the central registration in the Queen's Bench Division in London. The Law Commission for England and Wales has recommended the repeal of the bills of sale legislation and replacement with a new "goods mortgages" regime and a Bill implementing the recommendations was announced in the 2017 Queen's Speech.

Book debts. Debts owed to a business for goods or services supplied on credit. Synonymous, or roughly so, with "receivables".

Business Finance Report. Business Finance and Security over Moveable Property (Scottish Executive Central Research Unit, 2002).

BRIA. Business and Regulatory Impact Assessment. This accompanies this Report and is available on our website.

Cedent. A person who assigns. See also "Assignor".

Cession. Another word for assignation.

Cessionary. Another word for assignee.

Charge. A term of English law. In a broad sense it means any security right. In a narrow sense it means an "equitable" security right. Nowadays the term is sometimes also used in Scotland, in the broad sense. In Scotland it is also used in the expression "floating charge."

Chargeback. A security granted by a bank customer to the bank over the credit balance on an account with that bank.

Chattel. A concept of English law. Chattels divide into personal chattels (choses in possession) and real chattels (non-freehold non-equitable interests in land, eg leases). If

used without an adjective, "chattel" means personal chattel. A chattel mortgage is a mortgage of a personal chattel effected by a "bill of sale".

Choses in action and choses in possession. Concepts of English law, corresponding fairly closely to incorporeal and corporeal moveable property respectively in Scotland. See "personal property". In statutes, but seldom elsewhere, they are called "things in action" and "things in possession".

City of London Law Society draft Secured Transactions Code. A draft code for English secured transactions law prepared by the Financial Law Committee of the City of London Law Society, first published in July 2015. A revised version was issued in July 2016. See http://www.citysolicitors.org.uk/attachments/article/121/Draft%20Secured%20Transaction%20Code%20-%20Commentary%20-%20July%202016.pdf.

Claim. A personal right to the performance of an obligation, for example to payment of money. A claim is thus a debt, but viewed from the creditor's standpoint. A claim is typically based in contract. For example, the creditor's right arising out of a loan contract, or the seller's right arising out of a contract of sale. But a claim can arise for other reasons, for example a damages claim arising out of a delict. "Claim" is sometimes used to mean the assertion of a right that may be contested by others, such as an insurance claim or a damages claim, but in this Report the word is used in the sense described, ie a personal right to the performance of an obligation.

Close match search. A search system which allows some latitude for mistakes. For example, a search against "Joan Smith" will retrieve "John Smith". Contrast "exact match search".

Collateral. Property that stands as security for a debt. Thus if someone pledges a gold ring to a pawnbroker, the ring is collateral for the loan that the pawnbroker makes. Collateral may be corporeal property, as here, or incorporeal property.

Company charges registration regime. Part 25 of the Companies Act 2006 (and before it its predecessors, most recently Part XII of the Companies Act 1985) requires that certain security rights ("charges") in which the debtor is a company must be registered in the Companies Register within 21 days of their creation, on pain of invalidity against certain parties. Also applies to LLPs. Significant changes were made to the regime with effect from 1 April 2013.

Companies Register. Each company registered under the Companies Acts has its own file. We refer to the totality of these files as the "Companies Register", though that term is not used in the Companies Acts. Most types of security rights granted by a company must be registered in this register: this is the "company charges registration regime". There are three such registers (England and Wales, Scotland, Northern Ireland), each with its own Registrar, though in practice they are closely connected, and share a website at https://www.gov.uk/government/organisations/companies-house.

Completion of title. The final step whereby a right is acquired. For example in the acquisition of land, title is completed by registration. In an assignation of a claim, title is completed by intimation.

Conditional sale. The same as sale with retention of title. The term "conditional sale" tends to be used in consumer transactions.

Corporeal moveable property. Tangible property which is not land, such as equipment and vehicles.

Correction. An alteration or deletion of an entry in the Register of Assignations or Register of Statutory Pledges to reflect the correct legal position, for example to remove an entry which has resulted from a frivolous or vexatious registration.

Crowther Report. The Report of the Committee on Consumer Credit, 1971 (Cmnd 4596), chaired by Geoffrey Crowther. It was partially implemented by the Consumer Credit Act 1974. Part 5 of the Report, recommending the adoption of legislation based on UCC–9, was not implemented.

Crystallisation. The effect of a floating charge is suspended until such time, if any, as it crystallises. Crystallisation can happen in three ways: (i) liquidation, (ii) administration and (iii) receivership. (But whilst liquidation and receivership always imply crystallisation, administration does not necessarily imply it.) "Crystallisation" is the term used in England, and commonly used also in Scotland, though the legislation does not use this word, but rather "attachment".

DBEIS. Department for Business, Energy and Industrial Strategy. Successor Department of the UK Government to "DBIS".

DBIS. Department for Business, Innovation and Skills. Succeeded by "DBEIS" in 2016.

DCFR. C von Bar and E Clive (eds), *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR)* (2010). The full version is in six volumes. A one-volume outline edition is also available in print and at <http://ec.europa.eu/justice/policies/civil/docs/dcfr_outline_edition_en.pdf>. Book IX covers secured transactions over corporeal and incorporeal moveable property. Strongly influenced by UCC–9 and the PPSAs.

Debt. The same as a claim, but viewed from the standpoint of the debtor. However, sometimes in practice the word "debt" is used in both senses. For example, one may read of "the sale of a debt", meaning not the sale of the debt by the debtor (which would not be possible) but the sale of the claim by the creditor.

Debtor. The person who owes the debt. Normally this person and the person who grants the security right are the same, as is usually the case. In fact it is competent for one person to grant security in relation to another's debt. For this reason, some legislative texts avoid the word "debtor" to mean the granter of the security, and use other terms, such as "security provider" (DCFR) or "charger" (EBRD) or "obligor" (UNIDROIT Principles of International Contracts (2010)). UCC–9 and some PPSAs use "debtor" but define it to include granter of the security. (Eg UCC § 9–102(28)(A).) The draft Moveable Transactions (Scotland) Bill uses the term "provider" for the granter of a pledge.

***Delectus personae*.** Literally, selection of the person. There are two kinds. (i) *Delectus personae creditoris*. This, "selection of the person of the creditor", means that that person

cannot assign to someone else, so that the other party's obligations are owed solely to the original right-holder. The doctrine thus bars the transfer of personal rights. (ii) *Delectus personae debitoris*. This, "selection of the person of the debtor", bars sub-contracting, ie the obligant must perform personally, and cannot perform by the hand of another. Whether there is *delectus personae* of either type depends on the facts and circumstances of the case.

Department of the Registers of Scotland. Also called "Registers of Scotland" or simply "RoS". A non-ministerial Government department (with a staff of about 1400) that is headed by the Keeper of the Registers of Scotland and holds 18 registers. See https://www.ros.gov.uk/.

Diamond Report. A L Diamond, *A Review of Security Interests in Property* (Department of Trade and Industry, 1989), recommending the adoption of legislation broadly based on Article 9 of the UCC. It was not implemented.

Diligence. The set of procedures whereby an unpaid unsecured creditor can enforce the claim against the assets, corporeal and incorporeal, of the debtor. For example, X owes money to Y and Y owes money to Z. Z obtains decree for payment against Y. The debt owed by X is an asset in Y's patrimony. To enforce this decree, Z can "arrest in the hands of" X, thereby attaching the claim. The subsequent step of "furthcoming" results in payment by X to Z, not to Y. Other forms of diligence also exist, according to the type of asset in question.

EBRD. European Bank for Reconstruction and Development. Its *Model Law on Secured Transactions* was devised as a model for legislation in the post-communist states of central and eastern Europe. It was strongly influenced by the UCC–9 and the PPSAs, but was adapted for use within a corpus of civilian private law. Available at http://www.ebrd.com/pages/research/publications/guides/model.shtml. The *Core Principles for a Secured Transactions Law* underlying the model law can be found at http://www.ebrd.com/pages/sector/legal/secured/core/coreprinciples.shtml. There is also the EBRD publication *Publicity of Security Rights: Guiding Principles for the Development of a Charges Registry*, available at http://www.ebrd.com/downloads/legal/secured/pubsec.pdf.

Effective registration. A successful registration in relation to either (a) an assignation in the RoA which would be required for the relevant claim to be transferred by registration; or (b) a statutory pledge in the RSP which would be required to create (or amend) a statutory pledge.

Encumbered property. The asset or assets burdened by a pledge.

Equipment. See "inventory".

Equity/equitable. In English law, some rights have a double existence: they may exist "at law" or "in equity". (In the ordinary sense of the word "law" they are both part of English law.) Rights in security can be either legal or equitable. In general, equitable security rights are created by simple agreement, without any external act. An equitable security is generally valid in the debtor's insolvency. But it is often defeasible, for example if the debtor sells the property to a *bona fide* purchaser. Thus it is often weaker than a legal security. The

legal/equitable distinction does not exist in Scottish law. "Equity" also means the market value of an asset, less the amount of debt secured over it. Thus if land is worth £1,000,000 and there is a standard security over it, securing a debt of £400,000, the "equity" of the property is £600,000.

Exact match search. A search system allowing little latitude for errors where only the precise words or numbers searched against will be retrieved. Contrast "close match search".

Express security. Also called voluntary security, or security *ex voluntate.* A security deliberately granted by debtor to creditor. The contrast is with securities arising by operation of law.

External act (or overt act). Where X conveys to Y, or grants a subordinate right to Y, the law usually provides that the X/Y contract is not the sole requirement. For the transaction to affect third parties, there must be some additional, "external", act. It may be delivery, or registration, or (in assignation) intimation. Where an external act is not required, the transfer, security etc is said to take effect *solo consensu*, ie by consent alone. An external act is called for to satisfy the publicity principle. "All rights in security … require for their constitution not only an agreement between the parties but some overt act." W M Gloag and J M Irvine, *The Law of Rights in Security, Heritable and Moveable, including Cautionary Obligations* (1897) 8. The term "external" act is used in this Report, but the meaning is the same as "overt".

Extract. Official copy of an entry in the Register of Assignations or Register of Statutory Pledges.

Factoring. Two main transaction types fall under this name. In both cases what is dealt with is the invoice book of a business. (i) The business may use the factoring company simply as an agent, to administer its receivables *etc*. In this type of factoring the invoices are not sold. What is happening is simply an outsourcing of part of the work of the business's accounts department. (ii) The business sells to the factoring company the invoices as they arise. Thus the business first sells the goods (or renders the services) and then immediately sells the invoices for those goods. There is an assignation to the factoring company, with notification to the customers. It is for agreement as to whether the risk of the insolvency of a customer is to be borne by the business or by the factor. (If by the business, the arrangement becomes difficult to distinguish from a secured transaction.) The term "factoring" is sometimes applied to the sale of receivables without notification, but this is more usually known as invoice discounting. The term is also occasionally used to refer to the use of invoices as loan collateral, but at present this practice does not seem to happen in Scotland.

FCARs. The Financial Collateral Arrangements (No. 2) Regulations 2003 (SI 2003/3226). See "financial collateral".

Fiducia cum creditore. Or more fully *fiducia cum creditore contracta*. Also called fiduciary transfer of title. Transfer of title from debtor to creditor, for the purpose of security. It is an example of improper security.

Filing. The term used in UCC–9 to mean registration. (A distinction is occasionally drawn between filing and registration. See eg Crowther Report para 5.7.13. But this distinction is not generally accepted.) See "registration".

Finance lease. Or financial lease. A lease of moveable property in which the term represents most of the useful life of the property. The contrast is with an "operating" lease in which the lease term is small compared to the lifespan of the property. The hire of a car for a week or for a month would be an example of an operating lease.

Financial collateral. Financial assets used as collateral. The subject is regulated by the Financial Collateral Directive (Directive 2002/47/EC as amended by Directive 2009/44/EC). This is transposed for the UK by the Financial Collateral Arrangements (No. 2) Regulations 2003 (SI 2003/3226) as amended by the Financial Markets and Insolvency (Settlement Finality and Financial Collateral Arrangements) (Amendment) Regulations 2010 (SI 2010/2993). The Directive and Regulations recognise two types of financial collateral arrangement: (a) a security financial collateral arrangement (SFCA) and (b) a title transfer financial collateral arrangement (TTFCA). See Chapters 14 and 37 below.

Financial instrument. The type of financial collateral over which a statutory pledge may be granted. Typical examples of financial instruments are company shares and bonds.

Financing statement. See "registration".

Fixed security. A security right other than a floating charge.

FLA. The Finance and Leasing Association.

Floating charge. A security right developed at common law (more precisely, in equity) in England in the nineteenth century and adopted by statute in Scotland in 1961. It can cover all assets of the debtor, present and future. It can cover immoveable as well as moveable property. Only certain entities can grant a floating charge, most importantly companies and LLPs. Unless and until it crystallises its effect is suspended. When the provider disposes of an asset, the charge automatically ceases to encumber the asset. If the provider becomes insolvent, its priority is weaker than that of other securities. Lenders commonly expect to be granted a floating charge, often in combination with other security rights. Governed partly by the Companies Act 1985 and partly by the Insolvency Act 1986. The provisions of the former are prospectively repealed and replaced by Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007, but it is now unlikely that this legislation will ever be brought into force.

Floating lien. In UCC–9 and the PPSAs, a security that covers after-acquired property while allowing the debtor to dispose of (at least some types of) assets in the ordinary course of business. (The term itself is not used in the legislation, which does not have a specific term.) It is functionally comparable to the floating charge but it does not cover immoveable property. It does not make use of the concept of crystallisation.

Future assets. See "after-acquired" assets.

Goods. (Almost always used in the plural.) The term can be used to refer to assets of any kind, but usually the term is limited to corporeal moveable property.

Halliday Report. *Report by the Working Party on Security over Moveable Property*, 1986, chaired by Professor John (Jack) Halliday and available on the SLC website. It was not implemented.

Hire-purchase (HP). X (eg a motor dealer) owns a corporeal moveable asset (eg a car). Y, a customer, lacks the resources to buy the car outright. X sells the asset to Z, a financier, and Z then hires it to Y, with an option for Y to acquire ownership by making full payment.

Hypothec. Non-possessory security over corporeal property. Whilst security over land is in principle a hypothec, in practice the term is used in Scotland only for moveable hypothecs ie non-possessory security over corporeal moveables. (By contrast in many countries the term is used mainly for land.) Scottish law does not generally allow moveable hypothecs. Exceptions are ship mortgages, aircraft mortgages, floating charges, agricultural charges and the landlord's hypothec. The last of these arises by operation of law. It is a security over the tenant's goods in the tenanted property, in security of the rent. It has been abolished in relation to residential and agricultural tenancies.

Improper security. See "proper security".

Incorporeal moveable property. Intangible property which does not relate to land, such as financial instruments and intellectual property.

Information request. A request made to a person registered as an assignee in the RoA or as the secured creditor in the RSP for information in relation to the assignation or statutory pledge which has been registered. Limited types of person are entitled to make such a request and to have it answered.

Intellectual property (IP). Examples include patents, trade marks and copyright.

International private law (IPL). Also called private international law, or the conflict of laws. The branch of law that deals with (i) the question of which legal system governs a given matter (eg whether a contract is governed by Scottish contract law or by Texas contract law) and (ii) which country's courts have jurisdiction to hear and determine a given matter (eg whether a dispute arising out of a contract is to be heard and determined by a Scottish court or by a Texas court). Each country has its own IPL. The different IPLs do not always dovetail. IPL operates within non-unitary states. For example, IPL issues arise as between England and Scotland. See Chapters 15 and 39.

Inaccuracy. A misstatement in an entry in the Register of Assignations or Register of Statutory Pledges.

Intimation. Notification of assignation to the account debtor. (Scottish lawyers are used to this term. But others often find it puzzling, for in ordinary speech to "intimate" is to hint, or suggest, as in Wordsworth's *Intimations of Immortality*.)

Inventory. Also called stock in trade. A business's corporeal moveable property intended for sale, or for processing and then sale. The contrast is with equipment, which is the remainder of a business's corporeal moveable property. Office equipment, vehicles etc are normally equipment. (But there are businesses that deal in office equipment, vehicles etc.)

Invoice discounting. The selling of invoices without notification of the account party, so that the invoice will be paid to the original creditor, who will then pass on the payment to the invoice buyer. It is for agreement as to whether the risk of the insolvency of a customer is to be borne by the business or by the factor. (If by the business, the arrangement becomes difficult to distinguish from a secured transaction.) Cf "factoring".

Juridical act. An act with legal consequences, such as an assignation of a claim or the creation, amendment, transfer or extinction of a security right.

Keeper of the Registers of Scotland. The official who heads the Department of the Registers of Scotland and in whose name all acts and decisions are made.

Landlord's hypothec. See "hypothec".

Lien. (i) In its standard meaning in Scottish law, a lien is a security over corporeal moveable property arising by operation of law. It presupposes possession by the creditor. An example would be the lien that a repairer has over the object repaired (eg a car) in respect of the repair bill. But, by way of exception, "maritime liens" are non-possessory. (ii) The word is sometimes used more broadly, especially in the USA, to mean any security right.

Liquidation. The insolvency process for companies and certain other corporations which ultimately results in the extinction of the corporation. The person who administers a liquidation is called the liquidator.

LLP. Limited liability partnership. See the Limited Liability Partnerships Act 2000. Not to be confused with limited partnerships which are regulated by the Limited Partnership Act 1907.

LR(S)A 2012. Land Registration etc. (Scotland) Act 2012. The statute which regulates the Land Register of Scotland.

Mandate. A type of agency where the agent is not paid. Sometimes the mandate may be in the interest of the person (mandatory) to whom it is granted, as, typically, with a mandate to collect a debt.

Mature. If X lends Y money on 1 February, payable on 1 November, the claim "matures" on the latter date. Until then it is "unmatured", unless before that date it is "accelerated." The loan contract may provide for early repayment, in defined circumstances, and this is known as acceleration.

Moveable property. Property other than immoveable (also called heritable) property. The latter means land and what is connected with land, such as buildings, and also rights connected with land, such as the lease of a building. As well as being divided into moveable and immoveable/heritable, property is also divided into corporeal and incorporeal. Examples of incorporeal moveable property include receivables and intellectual property.

Murray Report. *Security over Moveable Property in Scotland: a Consultation Paper* (Department of Trade and Industry, 1994). Produced for the DTI by an advisory group chaired by Professor John Murray. Strictly this was a consultation paper rather than a report, so that "Murray Report" is not an accurate title, but nevertheless the paper came to be known by that name, perhaps because it contained a draft Bill. No final report was

published. No legislation resulted, but some of the ideas were echoed in Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007.

Negotiable instrument. A document that goes beyond evidencing a debt, and "embodies" it. The main types of negotiable instrument are the bill of exchange (also called the draft) and the promissory note. Negotiable instruments are more easily transferable than other claims. Notification to the account debtor is not required. The doctrine of *assignatus utitur jure auctoris* does not generally apply to them, so that a good faith transferee generally takes free of defences against payment. (The basic law of negotiable instruments is similar in all countries, as a result of their frequent use, over many centuries, in international trade. But the UK is not a party to the 1930 Bills of Exchange Convention. The Bills of Exchange Act 1882 continues in force.)

***Nemo plus juris ad alium transferre potest quam ipse haberet*.** (Ulpian, Dig 50.17.54.) Nobody can grant a larger right than is held by the granter. The same idea is sometimes expressed as *nemo dat quod non habet*. Thus if X borrows a bicycle from Y and then (fraudulently) sells it to Z, Z has no title. The principle applies even if the grantee is in good faith, but subject to certain exceptions, notably sections 24 and 25 of the Sale of Goods Act 1979. See also "accretion of title."

Non-notification security. Security over a claim without notification to the account debtor. This is competent under current law only in the case of the floating charge.

Non-possessory security. Security over corporeal property in which the debtor retains possession. That is always the case for security over corporeal immoveable (heritable) property. Scottish law currently allows this for corporeal moveable property only in certain cases, namely the floating charge, the agricultural charge, the landlord's hypothec and certain maritime security rights.

Noting filing/registration. See "registration".

Operation of law. A security that arises "by operation of law" is one that comes into existence automatically in defined circumstances, without having to be granted to the creditor by the debtor. Also called a security *ex lege*, or a "tacit" security. An example is the repairer's lien. Thus a garage that repairs a motor vehicle has, in respect of the repair bill, a security over the vehicle, arising by operation of law. The contrast is with "express" security.

Outright assignation. See "assignation".

***Pactum commissorium*.** Also called a *pactum legis commissoriae*. A clause in a secured loan contract whereby in the event of default, title to the collateral passes to the creditor. In most legal systems, including probably Scotland, such clauses are normally void.

Part 25 of the Companies Act 2006. See the "company charges registration regime".

Perfection. A term used in UCC–9 and the PPSAs. In those systems, a security interest attaches when it is effective as between debtor and creditor, but at that stage it is not (subject to certain exceptions) effective against third parties. The next step is perfection, whereby the security interest becomes effective against third parties (subject to certain

exceptions). Perfection usually requires either (i) registration or (ii) possession, but there are exceptions.

Person. In law a person is the subject of rights and obligations. So as well as (i) natural persons, such as David Hume or Rob Roy MacGregor, there are (ii) juristic persons (also called legal persons) such as companies.

Personal Property. Or "personality". A term of English law, corresponding closely to the concept of moveable property. Personal property divides into "choses in possession" (also called tangible property) and "choses in action" (also called intangible property), corresponding approximately to the division between corporeal and incorporeal moveable property. The word "personal" in the phrase "personal property" is not the same as the concept of personal right.

Personal Property Security Acts (PPSA). Statutes based on UCC–9 are often called Personal Property Security Acts and in Australia and New Zealand as the Personal Property *Securities* Acts. In this context the word "personal" is used to mean "moveable". Whereas Article 9 is merely one part of a general commercial code, the PPSAs are free-standing enactments. The PPSAs differ to some extent from the UCC and also to some extent vary among themselves, but the similarities outweigh the differences. In Australia the PPSA has been adopted at Commonwealth (ie federal) level so that the law is the same in the different states. In Canada the law has been adopted at provincial level, so there is some variation within Canada. Quebec is the exception, but the legislation there has in fact been much influenced by the PPSAs. The links for the legislation in Australia, New Zealand, Ontario and Saskatchewan are as follows:
http://www.comlaw.gov.au/comlaw/management.nsf/lookupindexpagesbyid/IP200944081?OpenDocument;
http://www.legislation.govt.nz/act/public/1999/0126/latest/DLM45900.html;
http://www.e-laws.gov.on.ca/html/statutes/english/elaws_statutes_90p10_e.htm; and
http://www.qp.gov.sk.ca/documents/English/Statutes/Statutes/P6-2.pdf.

Personal right. A right against a person. Also called a claim. Contracts create personal rights, but such rights can also have other sources. A personal right is as good as the person against whom it is held. A personal right against the Bank of England to be paid £1 is better than a personal right for the same amount against a person who has become insolvent. A right may still be personal even if it relates to property. For example if X owns land and contracts to transfer it to Y, Y's right is personal. A real right is a right directly in a thing rather than against a person. Thus when Y's name replaces X's in the Land Register, Y has a real right, and the personal right against X is now spent. Real rights are as good as the thing in which they are held.

Pledge. Under the current law, pledge is a security over corporeal moveable property constituted by delivery to the creditor. For example if Jack goes to a pawnbroker, and borrows money on the security of an antique clock that he hands over the counter, the clock has been given in pledge as security for the loan. Occasionally the term is used in a broader sense to mean any kind of security right. Under our recommendations a new form of pledge, to known as a "statutory pledge" would be introduced to complement the existing (possessory) pledge.

Possession. To be distinguished from ownership. To quote Ulpian: "*Nihil commune habet proprietas cum possessione*." (Dig 41,2,12. "Ownership and possession have nothing in common with each other.") Whilst ownership and possession commonly coincide, there are non-possessing owners and non-owning possessors.

Possessory security. Security over corporeal property in which the security is based on the possession of the creditor. Pledge and lien are the possessory securities under the current law, the difference between them being that pledge is express (voluntary) and lien is tacit (implied by operation of law).

PMSI. See "purchase money security interest".

PPSA. See "Personal Property Security Acts (PPSA)".

PPSR. Personal Property Security Register. See "Personal Property Security Acts (PPSA)".

***Prior tempore potior jure*.** Earlier by time, stronger by right. For example, if there are two securities over an item of property, held by different creditors, the first to be created has a higher rank than (has priority over) the second. That is an example where the competing rights can both exist, and the only question is of ranking. Sometimes the competing rights cannot co-exist, so that the first excludes the second wholly. For example, X assigns a right to A and to B. The first to complete title by intimating to the account debtor excludes the other.

Priority circle. Where ranking rules provide a circular result. For example, creditor A ranks above creditor B, creditor B ranks above creditor C, but creditor C ranks above creditor A. It is necessary in such circumstances is to find a way of breaking the circle.

Proper security. A security right that is a subordinate right, leaving the title in the provider. Also known as a "true security". By contrast in an improper security title is vested in the creditor, and the debtor has a personal right against the creditor to acquire the title when the debt is paid.

Provider. The person granting a security right. Normally, but not always, that person would be the debtor in the obligation secured by the security right.

Publicity principle. The principle that what affects third parties should be discoverable by third parties. It is not an absolute principle. Different legal systems apply the principle with varying degrees of enthusiasm.

Purchase money security interest (PMSI). A right in security that secures the financing of the purchase of the asset over which the financing is itself secured. In UCC–9 and the PPSAs, a PMSI has priority over earlier security rights, held by other creditors, that cover after-acquired assets. Depending on whether the financing is provided by the seller or by a third party, a PMSI can be either (i) a seller-credit PMSI, where the goods are sold on credit or (ii) a lender-credit PMSI, where a lender such as a bank lends the buyer the money.

Quasi-security. This term is sometimes used to describe devices that have an effect similar to security, such as retention of title in sale, and hire-purchase.

R3. The Association of Business Recovery Professionals' (R3) Scottish Technical Committee.

Real right. See also "personal right". Real rights divide into (i) ownership and (ii) the subordinate real rights, or limited real rights, which are real rights held in something that is owned by someone else. For example if X owns land and borrows money from Y, granting a standard security to Y, there are now two real rights in the property, X's real right of ownership and Y's subordinate real right of security. A subordinate real right is also called a *jus in re aliena*.

Receivables. Also called trade receivables, or accounts, or accounts receivable, or book debts. Money due in respect of goods sold, or services rendered, on credit. The term is a commercial rather than a legal one, and its precise scope is open to debate.

Recharacterisation. In UCC–9 and the PPSAs, devices that function as security rights ("quasi-securities") are treated as security rights. Thus function prevails over form. So if X sells and delivers a bicycle to Y, retaining ownership until Y pays, that arrangement is "recharacterised" so that Y is treated as having become owner and X is treated as having a security interest. "Recharacterisation" is not a term used in these statutes themselves, but it is the standard label for this approach.

Register of Assignations. The new register to be administered by Registers of Scotland in which assignations of claims are registrable.

Register of Statutory Pledges. The new register to be administered by Registers of Scotland in which statutory pledges are registrable.

Registration. Also called filing. Sometimes registration is divided into "notice registration" and "transaction registration". The former, a feature of UCC–9 and the PPSAs, involves the registration of a skeletal "financing statement". This is different from the "security agreement" itself. The registered entry merely alerts third parties to the possibility that there may exist, or may exist in future, a security right. "Transaction registration" specifies the security right, and can involve registration of the security agreement itself. But the distinction between notice registration and transaction registration is not sharp. Registration can also vary in its nature in other respects. For example it can be a necessary condition for the creation of the security (the Scottish rule for security over land) or it can merely give notice of a security that has already been created off-register. The latter is the approach both of UCC–9 (and the PPSAs) and of Part 25 of the Companies Act 2006, though the consequences of non-registration are different in each case. One benefit of registration systems is that they can determine priority, and it is a common criticism of Part 25 of the Companies Act 2006 that (subject to certain qualifications) it fails to take advantage of this possibility.

Retention of title. Also called reservation of title, retention of ownership etc. If goods are sold and delivered on credit, the seller's position can be protected by retention of ownership (title). The sale contract says that ownership (title) is retained by the seller, notwithstanding delivery, until the price is paid. Also called conditional sale. In practical terms the effect is somewhat similar to an unconditional sale plus (i) a seller-to-buyer loan of the price, plus (ii)

buyer-to-seller payment of the price (out of the notional loan), plus (iii) with a grant back to the seller, by the buyer, of a security right over the goods, to secure the loan.

Retrocession. If X assigns to Y, and later Y assigns back to X, that re-assignation is commonly called "retrocession". The main case of retrocession in practice is where a right has been assigned in security of a loan, and the loan is later paid off.

RoA. See "Register of Assignations".

RoA Rules. Subordinate legislation which would regulate the RoA and related matters.

RSP. See "Register of Statutory Pledges".

RSP Rules. Subordinate legislation which would regulate the RSP and related matters.

Section 893 order. A security right granted by a company generally has to be registered in the Companies Register under Part 25 of the Companies Act 2006. If the security is registered in another register anyway (for example, a standard security registered in the Land Register), the result is a requirement for double registration. Section 893 of the 2006 Act is an innovation allowing the Secretary of State to make an order whereby registration in the "special" register (eg the Land Register) suffices, though in that case the information is passed on to the Companies Register. The benefit to the parties is that only one registration is needed to protect the validity of the transaction. So far no section 893 order has been made.

Secured Transactions Law Reform Project. A project working to reform the law of secured transactions in England and Wales. See https://securedtransactionslawreformproject.org/.

Securitisation. The sale of financial assets from the original creditor ("originator") to a "special purpose vehicle" (SPV) which funds the purchase by issuing bonds. Sums due on mortgage (heritable security), credit cards, car loans etc are securitised. Securitisation may be effected by assignation, though in current practice this is uncommon. But sale without actual transfer is more common. Securitisation is a business term rather than a legal term. In legal (but not business) terms, securitisation is similar to factoring.

Security agreement. The term used in UCC–9 and the PPSA systems to mean the agreement that constitutes the security right. In those systems it is distinct from the "financing statement", the latter being the document that is registered.

Security. This term has two meanings, which have little connection. (i) A right in security, ie a right that secures some other right, such as a security over land that secures payment of a loan. "Security" in that sense is the subject of much of this Report and we generally therefore use the term "security right". (ii) Company shares, bonds etc ie financial instruments. This second sense is not a precise one. For example the Banking Act 2009 uses the term to include "any … instrument creating or acknowledging a debt." (Section 14.)

"Seriously misleading" test. If there was an inaccuracy in an entry in the RoA or RSP which was seriously misleading at the time of registration the registration would be ineffective. The result would be that the assignation would not transfer the claim or no

statutory pledge would be created. In the RSP there would be protection given to good faith acquirers where an entry had a supervening inaccuracy which was seriously misleading.

Sequestration. Commonly known as bankruptcy. The insolvency process available for types of debtor other than companies and LLPs, for which liquidation is the appropriate process. The person who administers a sequestration is called the trustee in sequestration.

SFCA. Security financial collateral arrangement. See "financial collateral".

Ship mortgage. A non-possessory security over a ship, created by registration. See the Merchant Shipping Act 1995 Sch 1.

Situs. The place where an asset is situated for the purpose of determining which legal system is applicable to it. The *situs* of land is the country where the land is. The same is generally true of corporeal moveable property. Incorporeal property has no *situs* in a literal sense, but a *situs* has to be allocated to it for certain purposes. For example if Scottish company X lends money to Scottish company Y, the resulting monetary claim is an asset of X: it is incorporeal moveable property with a Scottish *situs*. The law of the *situs* is known as the *lex situs* or the *lex rei sitae*.

Solo consensu. By consent alone. A transfer, or a security, that works *solu consensu* is one that requires no external act.

Standard security. A right in security in land is called a "heritable security". (The English equivalent is a mortgage.) The only type of heritable security competent in modern law is the standard security. It gives the grantee a limited right in the property, leaving ownership with the granter. (Conveyancing and Feudal Reform (Scotland) Act 1970.) Created by registration in the Land Register.

Statutory pledge. A new type of pledge which would require registration in the Register of Statutory Pledges for creation. It would be a non-possessory security in relation to corporeal moveables. It would be available for limited classes of incorporeal moveables, namely financial instruments and intellectual property.

Statutory pledges record. The main part of the Register of Statutory Pledges.

Supervening inaccuracy. Where a register entry becomes inaccurate by reason of a subsequent event.

Tacit. See "operation of law".

True security. See "proper security".

Trust receipt financing. Imported goods are often paid for not by the importer but by a bank (under a letter of credit), with the importer later repaying the bank. Under such an arrangement the bill of lading is sent by the exporter not to the importer but to the bank. The bank will not normally release the bill of lading to the importer except in exchange for payment. However, this letter of credit system can be extended by trust receipt financing, in which the importer receives the bill of lading from the bank without first paying. The importer gives the bank a document called a trust receipt (often abbreviated to TR), whereby it holds

the bill of lading, and the goods it represents, on behalf of the bank until payment is eventually made. In UCC–9 and the PPSAs a trust receipt is classified as a non-possessory security interest and therefore subject to the usual perfection requirements.

TTFCA. Title transfer financial collateral arrangement. See "financial collateral".

UCC. **(**The Uniform Commercial Code of the USA.) Available at http://www.law.cornell.edu/ucc/ucc.table.html. The UCC is divided into parts called articles. Article 9 deals with security interests in moveable property and is in this Report cited as "UCC–9". The UCC is a model law, which has been enacted in virtually identical form by all fifty states. (Except Louisiana, which has not adopted the whole of the UCC. But it has adopted Article 9.) It is revised from time to time, and in practice the states adopt the revisions promptly.

UCC–9 and the PPSAs. This term is used in this Report to indicate the PPSA systems, and Article 9 of the UCC, from which the PPSAs took their inspiration. The PPSAs differ to some extent from the UCC, and also differ among themselves. Moreover, all of them are amended from time to time. Hence the expression "UCC–9 and the PPSAs" does not signify some unique and unchanging system, but rather a broad approach.

UNCITRAL. The United Nations Commission on International Trade Law.

UNCITRAL Assignment Convention. The UNCITRAL Convention on the Assignment of Receivables in International Trade. Available at https://www.uncitral.org/pdf/english/texts/payments/receivables/ctc-assignment-convention-e.pdf.

UNCITRAL Guide on the Implementation of a Security Rights Registry. A set of recommendations published by UNCITRAL in 2014 on setting up a security rights registry. Available at http://www.uncitral.org/pdf/english/texts/security/Security-Rights-Registry-Guide-e.pdf.

UNCITRAL Legislative Guide on Secured Transactions. A set of recommendations by UNCITRAL as to what national laws about secured transactions should look like. Available at http://www.uncitral.org/uncitral/en/uncitral_texts/payments/Guide_securedtrans.html. The main Guide dates to 2007 and was supplemented in 2010 by a Supplement on Security Rights in Intellectual Property, available at http://www.uncitral.org/pdf/english/texts/security-lg/e/10-57126_Ebook_Suppl_SR_IP.pdf.

UNCITRAL Model Law on Secured Transactions. A set of model statutory provisions on secured transactions published by UNCITRAL in 2016 and available for adoption for countries seeking a modern secured transactions law. The approach taken is a functional one similar to UCC–9 and the PPSAs. Available at http://www.uncitral.org/pdf/english/texts/security/ML_ST_E_ebook.pdf.

UNIDROIT Cape Town Convention. International Institute for the Unification of Private Law (UNIDROIT) Convention on International Interests in Mobile Equipment. "Mobile equipment" means "(a) airframes, aircraft engines and helicopters; (b) railway rolling stock; and (c) space assets". Available at http://www.unidroit.org/instruments/security-interests/cape-town-

convention. The Convention itself is a framework convention, which works in unity with its protocols. Three protocols so far exist, for aircraft: (http://www.unidroit.org/instruments/security-interests/aircraft-protocol), railway rolling stock (http://www.unidroit.org/instruments/security-interests/rail-protocol) and space assets (http://www.unidroit.org/english/conventions/mobile-equipment/spaceassets-protocol-e.pdf). There are separate international registries for each of the three categories of asset. The UK acceded to the aircraft protocol on 1 November 2015. Work has commenced on a fourth protocol on agricultural, construction and mining equipment (the "MAC Protocol").

UNIDROIT Factoring Convention. International Institute for the Unification of Private Law (UNIDROIT) Convention on International Factoring. Available at http://www.unidroit.org/english/conventions/1988factoring/main.htm.

Verification statement. A statement issued to an applicant confirming that there has been registration in the RoA or RSP.

Warrandice. A warranty, or guarantee. If X assigns to Y money owed by Z, X is presumed to warrant to Y that the debt is indeed owed by Z. That is known at common law as warrandice *debitum subesse* – warrandice that the debt subsists. Such warrandice is only that the debt is payable, not that it will in fact be paid. For instance, if Z becomes bankrupt, that would not constitute breach of the warrandice. (But an additional guarantee about Z's solvency could be added, if X and Y so agree.) The exact content of warrandice in relation to the assignation of claims is uncertain and in this Report we recommend a clear statutory rule.

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: D L Carey Miller with D Irvine, *Corporeal Moveables in Scots Law* (2nd edn, 2005)

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: R C C Cuming, C Walsh and R J Wood, *Personal Property Security Law* (2nd edn, 2012)

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Chapter 1 Introduction

The importance of moveable transactions law

1.1 A successful modern economy is facilitated by a commercial law which meets its needs.[1] Recent years have seen this Commission carry out projects which have had the strategic objective of improving our commercial law. Several of these have now been implemented by legislation. The Legal Writings (Counterparts and Delivery) (Scotland) Act 2015 and the Contract (Third Party Rights) (Scotland) Act 2017 are the most recent examples.[2]

1.2 It is arguable that the area of Scottish commercial law where reform is longest overdue and most needed is moveable transactions law.[3] We shall explain this term in more detail below, but at the heart of it is the transfer of rights to be paid money, and security over moveable property.

1.3 The law here is of great importance primarily to businesses but also to private individuals seeking to use their assets to raise finance. Thus, a business may wish to acquire funding by selling debts due to it,[4] for example to factoring and invoice discounting houses. Alternatively, it may wish to retain assets such as vehicles, equipment and intellectual property, but use these as collateral to obtain loan finance. The purpose of the collateral is to protect the lender if the business becomes insolvent or otherwise fails to repay the loan. This enables lenders to offer reduced interest rates because the risk to them is lower, meaning reduced costs for the business.[5]

1.4 The internationally-respected UNCITRAL Legislative Guide on Secured Transactions considers that:

> "sound secured transactions laws can have significant economic benefits for States that adopt them, including attracting credit from domestic and foreign lenders and other credit providers, promoting the development and growth of domestic

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[1] See eg Lord Hodge, "Does Scotland needs its own Commercial Law?" (2015) 19 EdinLR 299 at 305 where it is stated that we must ask "how best our law can serve the business community by facilitating commercial activity." See also Lord Thomas of Cwmgiedd, "Developing commercial law through the courts: rebalancing the relationship between the courts and arbitration", The Bailii Lecture, 9 March 2016 para 4: "Clarity and predictability in the law, as well as its ability to develop in a principled manner, is the bedrock upon which businesses, just as much as individuals, order their affairs". Available at https://www.judiciary.gov.uk/wp-content/uploads/2016/03/lcj-speech-bailli-lecture-20160309.pdf.

[2] The 2015 Act implements our Report on Formation of Contract: Execution in Counterpart (Scot Law Com No 231, 2013). The 2017 Act implements our Review of Contract Law: Report on Third Party Rights (Scot Law Com No 245, 2016).

[3] See eg Gloag and Irvine, *Rights in Security* 187–188; D O'Donnell and D L Carey Miller, "Security over Moveables: A Longstanding Reform Agenda in Scots Law" 1997 *Zeitschrift für Europäisches Privatrecht* 807 and I G McNeil (ed), *Scots Commercial Law* (2014) para 11.94 (J MacLeod).

[4] The Scottish economist Henry Dunning Macleod (1821-1902) has commented: "If we were asked – who made the discovery which has most deeply affected the fortunes of the human race? We think, after full consideration, we might safely answer – the man who first discovered that Debt is a Saleable Commodity." See H D Macleod, *The Principles of Economic Philosophy* (2nd edn, 1872) 481.

[5] See eg G McCormack, "Secured transactions law reform, UNCITRAL and the export of foreign legal models" in N O Akseli (ed), *Availability of Credit and Secured Transactions in a Time of Crisis* (2013) 33 at 49–50.

businesses (in particular small and medium-sized enterprises) and generally increasing trade. Such laws also benefit consumers by lowering prices for goods and generally increasing trade."[6]

1.5 Our current law falls well short of meeting these standards. It is primarily common law (non-statute law) and is outmoded, inadequate and inflexible.[7] This puts barriers in the way of business and makes Scotland contrast unfavourably with other jurisdictions which have recognised the need for reform to promote more economic efficiency.[8] Deficiencies in our law may significantly hamper access to finance and we understand that some financiers simply do not engage in the Scottish market due to legal difficulties.

1.6 There is widespread dissatisfaction with the current law. CBI Scotland has stated that the "ease of [small and medium-sized enterprises] accessing credit is constrained in a way which would not be the case if they were English based."[9] The Federation of Small Businesses has said: "Today's small businesses need a commercial environment that lets them raise finance against business assets quickly and easily. The current law is rooted in the past and doesn't reflect how business is now done."[10] Lord Reed, a Justice of the UK Supreme Court, has commented that consideration should be given to whether certain Scottish businesses "are well served by legal rules which make it more difficult for them to raise finance" than under English law.[11] The assessment of Bruce Wood of Morton Fraser is more blunt: the law on moveable transactions is "an area of Scots law desperately in need of reform."[12]

1.7 That Scottish law remains unreformed in this area may affect the reputation of our legal system more generally. A Report on Business Finance and Security over Moveable Property for the then Scottish Executive in 2002 notes that solicitors are "embarrassed" to explain the Scottish rules in cross-border or international transactions.[13] Although this is anecdotal it is important. There is evidence to suggest that perceptions of the law as well as the actual underlying rules influence the availability of finance in a country.[14]

1.8 In this Report we make a series of recommendations for legislation to modernise our moveable transactions law. In our view these would enable it to meet the needs of business in the electronic age that is the twenty-first century. The introduction of a new Register of Assignations would enable assignation of rights to payment to be completed by registration, rather than there having to be intimation to the debtor as the current law requires. This

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[6] UNCITRAL Legislative Guide on Secured Transactions 1.
[7] See Chapter 3 below.
[8] See eg M Renaudin, "The modernisation of French secured credit law: law as a competitive tool in global markets" 2013 International Company and Commercial Law Review 385.
[9] Response of CBI Scotland to Discussion Paper on Moveable Transactions.
[10] Statement by Colin Borland, Senior Head of External Affairs, Devolved Nations to the Commission in December 2016.
[11] The types of business he was referring to were football and rugby clubs following the decision in *Joint Administrators of Rangers Football Club Plc, Noters* 2012 SLT 599, which is discussed below at para 3.16. See Lord Reed, "Triremes and Steamships: Scholars, Judges, and the Use of the Past", The Scrymgeour Lecture, University of Dundee, 30 October 2015, pp 9–10, available at https://www.supremecourt.uk/docs/speech-151030.pdf.
[12] *The Scotsman,* 28 August 2011, available at http://www.scotsman.com/news/it-s-an-area-of-scots-law-desperately-in-need-of-reform-1-1816927.
[13] Business Finance Report at 70. On this Report see paras 18.39–18.40 below.
[14] R Haselmann and P Wachtel, "Institutions and Bank Behaviour: Legal Environment, Legal Perception and the Composition of Bank Lending" (2010) 42 Journal of Money, Credit and Banking 966.

would significantly aid invoice financing, as well as allowing security over income streams such as rents to be taken more easily. Our recommendation for a new security right over moveable property, which would require neither transfer of ownership nor transfer of possession of that property, but only registration in the new Register of Statutory Pledges, would facilitate the use of such assets as collateral for loans. Taken together our recommendations would consign the restrictive rules of the current law to history.

1.9 Our overarching policy aims are simple ones: to improve access to finance in Scotland and benefit the Scottish economy by reforming the law of moveable transactions. We believe that this would assist the Scottish Government's National Outcome for Scotland to be the most attractive place for doing business in Europe.[15] For example, Jeff Longhurst, Head of Commercial and Asset Based Finance at UK Finance, has commented to us that a modern statutory framework for moveable transactions law would promote more invoice financing in Scotland and potentially encourage new finance companies to enter the Scottish market.

1.10 As is our usual practice, the Report is accompanied by a draft Bill, which is to be found in volume 3.

The three strands of the project

1.11 In the next section we outline the history of the moveable transactions project, but we think that it may assist the reader first to have an explanation of its three strands. We would refer also to the extensive Glossary at the start of the Report. The strands are:

(i) Outright transfer (assignation) of incorporeal moveable property;

(ii) Security over incorporeal moveable property; and

(iii) Security over corporeal moveable property.

1.12 In brief, "moveable property" is all property other than (a) land and buildings and (b) rights in land and buildings, such as leases. (The equivalent term in common law jurisdictions such as England and Wales, Canada, Australia and New Zealand is "personal property").[16] "Corporeal moveable property" is moveable property that has a physical presence, such as computers, equipment and motor vehicles. (In English law the term "chattels" is used.) "Incorporeal moveable property" is moveable property that does not have a physical presence, for example, company shares and intellectual property rights. (In English law the terms typically used are "choses in action" or "intangibles".)

1.13 Incorporeal moveable property also includes certain rights ("claims") against other persons, most importantly for present purposes, the right to be paid money by another person under a contract. For example, if Andrew sells goods to Barbara, he has a right to be paid the price by her. This right against Barbara can be regarded as a form of incorporeal moveable property.[17] Andrew is normally entitled to transfer that right to another person, for

[15] See http://www.gov.scot/About/Performance/scotPerforms/outcome/business.
[16] Hence the Personal Property Security Acts (PPSAs) which are mentioned throughout this Report.
[17] See Reid, *Property* para 16. But cf G L Gretton, "Ownership and its Objects" (2007) 71 Rabels Zeitschrift 802.

example a factoring company, which buys debts. The method of transfer of incorporeal property in Scotland is assignation. (The English law equivalent is "assignment".)

1.14 When the project's three strands are considered, there is an obvious lack of symmetry. Outright transfer of corporeal moveable property is not included. The reason for this is that the primary transaction involving such a transfer is sale. Sale of corporeal moveables is governed on a UK-basis by the Sale of Goods Act 1979.[18] In contrast, the other three strands are matters primarily regulated by Scottish common law. It would seem more appropriate to reform the Sale of Goods Act on a UK-wide basis, as indeed has happened by virtue of the Consumer Rights Act 2015.[19]

History of the project

1.15 The law relating to the assignation of, and security over, incorporeal moveable property was first identified as a project in our Seventh Programme of Law Reform, which ran from 2005 to 2009.[20] As can be seen, this project comprised two of the strands identified in the previous section. There was support for the project from several respondents to the consultation on the Seventh Programme. This included the Law Reform Committee of the Law Society of Scotland, which said that this area was "ripe for review". It added that it was important to ensure in cross-border issues that the Scottish legal system would not be ignored or that other systems which do provide some sort of security where Scottish law does not would be preferred over the Scottish system. Work on the project did not commence in earnest until our land registration project was completed. Our Report on Land Registration was published in February 2010[21] and subsequently implemented by the Land Registration etc. (Scotland) Act 2012. When we consulted in advance of our Eighth Programme of Law Reform, which ran from 2010 to 2014,[22] there was substantial support for extending the project to include the third strand identified above: security over corporeal moveable property. The then Lord President, Lord Hamilton, stated that the topic "appears to be in urgent need of consideration".[23] The WS Society said that this should be the first priority for the Commission in its Eighth Programme as there was "no workable fixed security in Scots law."[24]

1.16 The project was commenced under the leadership of Professor George Gretton, whose term of office as a Commissioner concluded in 2011. Our Discussion Paper was published in June of that year.[25] This was followed by our usual consultation period. Forty responses were received.[26] In October 2011 a symposium on the security aspects of the project (strands (ii) and (iii)) was held under the auspices of the Edinburgh Centre for Private Law at the University of Edinburgh. Over forty individuals attended and the speakers were Professor Gretton, Dr Ross Anderson, Dr Hamish Patrick and Professor Hugh Beale. Their

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[18] See Gretton and Steven, *Property, Trusts and Succession* paras 5.16–5.37 for an overview.
[19] This implements the Joint Report of the Law Commission and Scottish Law Commission on Consumer Remedies for Faulty Goods (Law Com No 317, Scot Law Com No 216, 2009) and the Joint Advice of the Law Commission and Scottish Law Commission on Unfair Terms in Contracts (2013).
[20] Scottish Law Commission, Seventh Programme of Law Reform (Scot Law Com No 198, 2005).
[21] Scottish Law Commission, Report on Land Registration (Scot Law Com No 222, 2010).
[22] Scottish Law Commission, Eighth Programme of Law Reform (Scot Law Com No 220, 2010).
[23] Submission of Lord President Hamilton to Consultation on Eighth Programme of Law Reform.
[24] Submission of WS Society to Consultation on Eighth Programme of Law Reform.
[25] Scottish Law Commission, Discussion Paper on Moveable Transactions (Scot Law Com DP No 151, 2011).
[26] See volume 3 of this Report. Following mergers etc, some of the law firm consultees which responded to the consultation no longer exist now in the same form as at the time of the consultation.

papers were subsequently published[27] and we have found these and the general discussion at the symposium very helpful in preparing this Report.

1.17 Following the end of the consultation period we had numerous meetings with consultees to discuss their responses. We met also with other stakeholders, including Registers of Scotland, Companies House, CBI Scotland, the Federation of Small Businesses, the Asset Based Finance Association,[28] the Finance and Leasing Association and the Consumer Credit Trade Association. These meetings were of considerable assistance, as were the frequent meetings which we had with our advisory group and with Registers of Scotland.[29] The size and complexity of the project led to it being carried forward to be completed as part of our Ninth Programme of Law Reform (2015 to 2017). In July 2017 we carried out a short consultation on the draft Moveable Transactions (Scotland) Bill. The comments of consultees greatly assisted us in preparing the final version of the draft Bill, which is appended to this Report.

Scope of project

1.18 Chapter 1 of the Discussion Paper[30] set out what is included and not included within the scope of the project. We do the same here, albeit more briefly.

(a) Outright assignation

1.19 As we noted above, "assignation" is the method by which incorporeal property is transferred in Scotland. But the project does not look at the law of assignation as a whole. First, its scope is generally restricted to the assignation of incorporeal *moveable* property. For the most part, we do not discuss the assignation of incorporeal *heritable* property, such as assignations of leases of land. Secondly, certain forms of incorporeal moveable property, such as the various types of intellectual property, negotiable instruments[31] and "securities", for example, company shares and bonds[32] have special transfer rules. This project does not seek to deal with these as they are distinct areas of law.

(b) Security rights

1.20 We do not cover tacit security rights, such as the repairer's lien, the seller's lien in the sale of goods and the landlord's hypothec.[33] Nor do we cover security rights created by diligence, such as the attachment of goods, or arrestment.[34] Rights of retention and rights of set off, though they have a security function, are also generally not included in this project, since they belong to the law of obligations.[35] As the project is limited to moveable property,

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[27] At (2012) 16 EdinLR 261.
[28] In July 2017 the Asset Based Finance Association became part of the newly established UK Finance. See https://www.ukfinance.org.uk/.
[29] See para 1.52 below.
[30] At paras 1.5–1.19.
[31] Most types of negotiable instrument are subject to the Bills of Exchange Act 1882, which sets out transfer rules in detail. These rules are largely the same as the common law rules for the transfer of negotiable instruments. A few types of negotiable instrument fall outwith the 1882 Act and the common law rules apply.
[32] See the Stock Transfer Act 1963, the Stock Transfer Act 1982 and the Uncertificated Securities Regulations (SI 2001/3755). The last of these is the legislative basis of the CREST system.
[33] See eg Gretton and Steven, *Property, Trusts and Succession* paras 21.58–21.65.
[34] See eg MacNeil (ed), *Scots Commercial Law* Ch 13 (F McCarthy).
[35] We are conducting a separate general review of contract law. See Scottish Law Commission, Ninth Programme of Law Reform (Scot Law Com No 242, 2015) paras 2.6–2.10. This includes retention and set-off.

security over heritable (immoveable) property is not dealt with. Our Ninth Programme includes a separate project on the law of heritable security and this will be carried forward to our Tenth Programme.[36]

1.21 Whilst, as mentioned above, this project does not deal with the *transfer* of the special types of incorporeal property such as intellectual property and negotiable instruments, we do cover *security* over these assets, in line with the position in comparator legislation.

(c) Quasi-security

1.22 Some transactions operate in a way that is similar to security. Common examples are retention of title, hire-purchase and trusts for security purposes. Such arrangements are sometimes called quasi-securities. Some jurisdictions take a "functional" rather than a "formal" approach to such arrangements and "recharacterise" them as security interests requiring registration.[37]

(d) Floating charges

1.23 The floating charge is a special form of security right generally only available to a limited number of corporate debtors, notably companies. Floating charges have been the subject of significant statutory reform provisions in the form of Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007, albeit the relevant provisions have never been brought into force.[38]

(e) International private law

1.24 Corporeal moveables, being mobile assets, can cross borders. As for incorporeals, they often have an international dimension, and moreover the question of how their *situs* (site) is to be determined for the purposes of the law of moveable transactions is problematic in a number of respects. In principle it would have been possible to address the international private law aspects of moveable transactions within this project. But we have taken the view that international private law issues should in general not be dealt with here. We have therefore decided to confine the project to the substantive (or internal) Scottish law of moveable transactions, leaving it to existing international private law to determine when Scottish law applies and when it does not. The reason for this approach was that the project needed to be kept within manageable bounds. We say more on this subject in Chapters 15 and 39.

(f) Comprehensive or selective?

1.25 The law of assignation of claims and the law of security over moveables are large subjects. A comprehensive review would take considerable time and resources. It seems to us preferable to identify the issues most in need of reform. Codification of this area realistically needs to be left to the future.

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[36] See Scottish Law Commission, Ninth Programme of Law Reform (Scot Law Com No 242, 2015) paras 2.15–2.17.

[37] In particular article 9 of the Uniform Commercial Code in the USA and the Personal Property Securities Acts in Canada and elsewhere.

[38] See Chapter 18 below.

(g) Insolvency law

1.26 The law of rights in security is closely linked to insolvency law. Nevertheless, this project is not about insolvency law and is thus intended to leave the policies of insolvency law substantially unaffected. This approach, which we set out in the Discussion Paper, met with opposition from some consultees and we address this in Chapter 18.

Comparative work

1.27 It is a standard part of law reform work to look at other jurisdictions and gain ideas.[39] In the field of moveable transactions law, there has been much to learn. The deficit that there is in Scottish law, when compared with the law of other countries, not least our nearest neighbours, England and Wales, becomes even clearer when this is done.

1.28 The landmark development in moveable transactions law in the twentieth century was the introduction of article 9 of the Uniform Commercial Code (UCC–9) in the USA.[40] This takes a functional approach to security over moveable property. Essentially any transaction carried out for security purposes will not be effective against third parties unless there has been a filing of a notice in a public register. UCC–9 heavily influenced the development of the Personal Property Security Acts (PPSAs), beginning in Canada. The last twenty years have seen PPSA-type legislation enacted in several jurisdictions, including New Zealand in 1999 and Australia in 2009. During a visit to these countries in 2012, the lead Commissioner learnt much about the experience there in relation to personal property security reform. We are particularly grateful to Professor Mike Gedye, University of Auckland, for his assistance with arranging meetings in New Zealand. In 2013 Malawi adopted a PPSA based on the New Zealand model.[41] In 2015, Nigeria enacted legislation which draws significantly on the UCC–9/PPSA approach.[42] And 2017 has seen similarly-influenced legislation passed in Zimbabwe.[43]

1.29 The UCC–9/PPSA approach also heavily influenced the Draft Common Frame of Reference (DCFR) Book IX.[44] The DCFR was an academic project which produced model provisions which might form the basis of a future statement of harmonised European private law. In one of our other current long-term projects, on contract law, we are using the DCFR as a means of providing Scottish law "with a systematic health check, giving a basis for treatment where the law is found to be ailing or otherwise in need of remedial treatment."[45] When one makes a cursory examination of the relevant DCFR provisions on moveable

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[39] See the Law Commissions Act 1965 s 3(1)(f). See also Sir Geoffrey Palmer QC, "The Law Reform Enterprise: Evaluating the Past and Chartering the Future" (2015) 131 LQR 402 at 415.
[40] See Discussion Paper, Chapter 13.
[41] See M Dubovec and C Kambili, "Secured Transactions Law Reform in Malawi: the 2013 Personal Property Security Act" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 183–206.
[42] See I Otabor-Olubor, "Reforming the law of secured transactions: bridging the gap between the company charge and CBN Regulations security interests" (2017) 17 Journal of Corporate Studies 39 and W C Iheme and S U Mba, "Towards reforming Nigeria's secured transactions law: the Central Bank of Nigeria's attempt through the back door" 2017 Journal of African Law 131.
[43] Movable Property Security Interests Act 2017. See https://www.zimlii.org/zw/legislation/act/2017/9.
[44] C von Bar and E Clive (eds), *Draft Common Frame of Reference: Principles, Definitions and Model Rules of European Private Law*, 6 vols (2009). On Book IX, see U Drobnig and O Böger, *Proprietary Security in Movable Assets* (2015).
[45] Scottish Law Commission, Ninth Programme of Law Reform (Scot Law Com No 242, 2015) para 2.6.

transactions law,[46] and then looks at Scottish law it immediately becomes apparent that major surgery is needed.

1.30 The DCFR Book IX has much influenced the new Belgian law on security over moveable property.[47] Even closer to home, Jersey has adopted a similar approach in its recent reform of security over intangibles.[48] The DCFR Book III chapter 5 deals with assignment.[49] We have found it very helpful in relation to assignation.

1.31 Mention should also be made of other transnational instruments which, although non-binding in the United Kingdom, provide models of modern law from which our project draws inspiration. These include the UNIDROIT Convention on International Factoring (1988); the European Bank for Reconstruction and Development's (EBRD) Model Law on Secured Transactions (1994); the UNCITRAL Convention on the Assignment of Receivables in International Trade (2001);[50] the UNCITRAL Legislative Guide on Secured Transactions (2007);[51] the UNCITRAL Guide on the Implementation of a Security Rights Registry (2014) and the UNCITRAL Model Law on Secured Transactions (2016).[52]

1.32 Over a decade ago, the Law Commission for England and Wales proposed reform of English law on the basis of the UCC–9/PPSA approach, but this was opposed by many working in the area and was not taken forward.[53]

1.33 We have also gained much from looking at current unreconstructed English law. It offers three key things which put Scottish law at a disadvantage.[54] First, in English law notification (intimation) to the account debtor is not necessary in order to assign a claim. In equity, C can assign to A his right to be paid money by B, without B having to be told. Intimation is commercially inconvenient as it increases transaction costs. Second, again in equity, it is possible to have a non-possessory security over chattels (corporeal moveables) known as a fixed charge. Thus the debtor can keep possession of the property. In

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[46] The provisions on assignation are in Book III and those on security are in Book IX. On Book IX, see Drobnig and Böger, *Proprietary Security in Movable Assets*.

[47] Pledge Act of 11 July 2013 which introduces a new title XVII to Book III of the Civil Code. This is expected to come into force on 1 January 2018. See E Dirix, "The New Belgian Act on Security Interests in Movable Property" (2014) 23 International Insolvency Review 171; F Helsen, "Security in Movables Revisited: Belgium's Rethinking of the Article 9 UCC System" (2015) 6 European Review of Private Law 959 and M Grégoire, "The Law of 11 July 2013 Amending the Belgian Civil Code with Respect to Security Interests in Movable Assets, and Repealing Various Provisions in this Area" in B Foëx (ed), *The Draft UNCITRAL* Model Law on Secured Transactions (2016) 171–198.

[48] Security Interests (Jersey) Law 2012. This is restricted to intangibles. Legislation on tangible movable property is expected to follow.

[49] See generally E Clive, "The Assignment Provisions in the Draft Common Frame of Reference" 2010 Juridical Review 275.

[50] See N O Akseli, "The United Nations Convention on the Assignment of Receivables in International Trade and Small Businesses" in Gullier and Akseli (eds), *Secured Transactions Law Reform* 465–479.

[51] This, for example, has influenced recent reform in Lithuania. See A Smaliukas, "Secured Transactions Law Reform in Lithuania" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 405 at 410.

[52] The Discussion Paper, Appendix A surveys those instruments pre-dating it. On the contribution of UNCITRAL see generally N O Akseli (ed), *Availability of Credit and Secured Transactions in a Time of Crisis* (2013). On the UNCITRAL Registry Guide, see G Castellano, "Reforming Non-Possessory Secured Transactions Laws: A New Strategy?" (2015) 78 MLR 611. On the UNCITRAL Model Law see B Foëx (ed), *The Draft UNCITRAL Model Law on Secured Transactions* (2016). And see also S V Bazinas, "The UNCITRAL Legislative Guide on Secured Transactions and the Draft UNCITRAL Model Law on Secured Transactions compared" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 481–502.

[53] This is discussed further in Chapter 18 below.

[54] See Discussion Paper, Appendix B.

Scotland, the only non-possessory security available is the floating charge, which, as we noted above,[55] is only available to certain corporate debtors and has a lower ranking in insolvency. Thirdly, it is also possible to take a fixed charge over incorporeal (intangible) assets such as financial instruments and intellectual property without transferring these to the secured creditor. Any sensible reform of moveable transactions law in Scotland requires to take account of these more business-friendly features of the law in its neighbouring jurisdiction.

1.34 But use of English law requires two health warnings. The first is that the underlying systems of property law north and south of the border are fundamentally different.[56] Caution must therefore be exercised. The importation of the floating charge to Scotland in 1961, whilst almost universally welcomed from a practical perspective, has proven to be problematic in its relation to other relevant areas of law.[57] Secondly, there is general consensus, despite the proposals of the Law Commission for the most part being unimplemented, that English law requires reform.[58] Some favour radical reform along the lines of UCC–9 and the PPSAs. Others favour a more conservative approach. Particular mention must be made of the work of the City of London Law Society[59] and the Secured Transactions Law Reform Project,[60] both of which are separately championing reform. We are grateful to these groups for their engagement with us. Mention must also be made of the work of the Law Commission for England and Wales on reform of bills of sale which has led to the Goods Mortgages Bill announced in the 2017 Queen's Speech.[61]

Two registers

1.35 The moveable transactions project has been one of the largest considered by this Commission. At the core of the scheme proposed in the Discussion Paper was the idea that a new register would be set up, to be known as the Register of Moveable Transactions (RMT), in which (a) assignations of claims; and (b) a new form of security right over moveable property would be registered. The scheme was broadly welcomed by consultees. When, however, we came to work up how the RMT would operate, it became increasingly

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[55] See para 1.22 above.

[56] See eg Reid, *Property* para 2. See also R G Anderson and J W A Biemans, "Reform of Assignation in Security: Lessons from the Netherlands" (2012) 16 EdinLR 24 at 31: "Because of the major role accorded to equity in the English security interest system, English law is of limited utility for Scottish law reformers."

[57] See Discussion Paper, Chapter 9. See also Chapter 17 below.

[58] The literature is large. See eg J de Lacy, "The evolution and regulation of security interests over personal property law" in De Lacy (ed), *Reform of UK Personal Property Security Law* 3 at 81–82; S Worthington, "How Secure is Security?" in L Gullifer and S Vogenauer (eds), *English and European Perspectives on Contract and Commercial Law: Essays in Honour of Hugh Beale* (2014) 417–437 and D Sheehan, *The Principles of Personal Property Law* (2nd edn, 2017) ch 15.

[59] See http://www.citysolicitors.org.uk/. The Financial Law Committee of the Society has now published three discussion papers, which are available on its website. On the first, which was published in November 2012 and is general in scope, see A J M Steven, "Secured Transactions Reform" (2013) 17 EdinLR 251. The second, published in February 2014, considered fixed and floating charges on insolvency. The third, published in July 2015, is a draft Secured Transactions Code. In July 2016 a revised version of the code was published for further comment. See also R Calnan, "What makes a good law of security?" in F Dahan (ed), *Research Handbook on Secured Financing in Commercial Transactions* (2016) 451 at 480–484.

[60] See http://securedtransactionslawreformproject.org/. On 17 November 2017, its Executive Director, Professor Louise Gullifer gave the Edinburgh Centre for Commercial Law Annual Lecture, with the title: "Secured Transactions Law Reform: The View from South of the Border". See also Gullifer and Akseli (eds), *Secured Transactions Law Reform*.

[61] See Law Commission, Bills of Sale (Law Com No 369, 2016). On 24 November 2017, when our Report was in the final stages of preparation, the Law Commission published From Bills of Sale to Goods Mortgages (Law Com No 376, 2017) which unfortunately came too late to be referred to elsewhere in our Report.

clear that the assignation and security parts would be distinct in character. This is because an assignation and a security are different types of transaction. An assignation is a *transfer* of a right whereas a security transaction involves the *creation* of a right. A security right once created can then be amended, transferred or extinguished. A register requires to take account of these further possible juridical acts in relation to the right. In contrast an assignation is a single juridical act. We came to the conclusion that rather than having one register with two distinctive parts, it would be preferable to have two separate registers.

Structure and content of the Report

1.36 This report is divided into three volumes. The present volume deals with reform of the law of assignation and the setting-up of the new Register of Assignations. Volume 2 considers reform of the law of security over moveable property and makes recommendations for establishing a new Register of Statutory Pledges. It lists also (a) those who responded to our Discussion Paper; (b) the members of our advisory group; (c) those who responded to our consultation on the draft Moveable Transactions (Scotland) Bill of July 2017 and (d) the considerable number of other people who have assisted us.

1.37 Volume 3 contains the draft Moveable Transactions (Scotland) Bill, which, if enacted, would give effect to the recommendations in the body of the Report.[62]

Legislative competence

Introduction

1.38 We noted in the Discussion Paper that under the Scotland Act 1998 the law of assignation is not reserved to the UK Parliament.[63] Neither is the law of rights in security.[64] They are part of the law of property. It, along with other areas including the law of obligations, is part of Scottish private law as defined in section 126(4) of the 1998 Act and is within the legislative competence of the Scottish Parliament. As Lord Hope of Craighead stated in *Imperial Tobacco v The Scottish Ministers*,[65] when considering the relationship between the law of obligations and the scope of the reservation in Schedule 5 to the 1998 Act, in relation to consumer protection and more particularly the regulation of the sale and supply of goods and services to consumers:

> "It would be surprising if the words used in section C7(a) ["The sale and supply of goods and services to consumers"] had such a wide reach. Responsibility for Scots private law, including the law of obligations arising from contract, belongs to the Scottish Parliament. This is made clear by section 29(4) which deals with modifications to Scots private law as it applies to reserved matters but leaves Scots private law otherwise untouched, and by the definition of what references to Scots private law are to be taken to mean in section 126(4). The sale and supply of goods

[62] There are a small number of technical provisions in the draft Bill which do not require recommendations in this Report.
[63] Discussion Paper, para 1.29.
[64] Note that floating charges and receivers are covered by an exception to the reservation of insolvency matters under the Scotland Act 1998 Sch 5 Part II Head C2 and the Scottish Parliament has already passed legislation on floating charges. See the Bankruptcy and Diligence etc. (Scotland) Act 2007 Part 2 (not in force) discussed in paras 18.23–18.25 below.
[65] [2012] UKSC 61.

is part of the law of obligations and, as such, is the responsibility of the Scottish Parliament."[66]

Consumer Credit Act 1974

1.39 The 1998 Act provides that the "subject matter of … the Consumer Credit Act 1974" is reserved.[67] The amendment to that Act which we recommend, enhancing the rights of consumers dealing with pawnbrokers,[68] would thus not fall within the legislative competence of the Scottish Parliament. But it is not an integral part of the whole reform scheme, which could thus go ahead in the Scottish Parliament whether or not Westminster was inclined to amend the 1974 Act.

1.40 The fact that some of our recommendations would relate to non-business debtors as well as to business debtors would not, to the extent that non-business debtors are consumers for the purposes of the 1974 Act, affect the subject matter of the 1974 Act. For example, the 1974 Act has general rules that cover all types of security right, where the security right is granted by a consumer debtor.[69] Those provisions would automatically apply to any new type of security right that would become competent under our recommendations, in so far as consumer debtors were involved.

1.41 The 1974 Act makes special provision for a pledge over corporeal moveable property (described as a "pawn") as part of the measures in that Act regulating credit agreements between consumers and pawnbrokers. The measures in our draft Bill therefore expressly do not affect the realisation of a pawn for the purposes of the 1974 Act.[70]

1.42 We recommend the creation of a new type of security right, to be known as a "statutory pledge".[71] Although any type of debtor, including consumer debtors, would be able to grant it, we recommend that its scope should be limited so that private individuals would not be able to use it as freely as business debtors. This limitation on the new security would not, in our view, be outwith the legislative powers of the Scottish Parliament.

Business associations

1.43 The law relating to "the creation, operation, regulation and dissolution of types of business association" is reserved.[72] Thus company law is in general terms outwith the legislative competence of the Scottish Parliament. Our recommendations would make it possible for a statutory pledge to affect moveable assets in general, including financial instruments such as company shares and bonds. We consider that where a debtor gives security to a creditor over certain assets, including shares held in a company, the security over the shares does not relate - except in an incidental manner - to "the creation, operation, regulation and dissolution of types of business association". It follows that a statutory pledge can be competently granted over company shares or bonds.

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[66] [2012] UKSC 61 at para 28.
[67] Scotland Act 1998 Sch 5 Part II Head C7.
[68] See paras 25.13–25.16 below.
[69] See para 27.15 below.
[70] See para 27.17 below.
[71] See Volume 2 of this Report.
[72] Scotland Act 1998 Sch 5 Part II Head C1.

Corporate insolvency law

1.44 Corporate insolvency law too is largely reserved.[73] As noted above,[74] insolvency law is in principle outwith our scope, although some of our consultees took issue with this. We have generally held to this approach. The fact that we wish our draft Bill to be within the competence of the Scottish Parliament is also a consideration in this regard.[75] It follows that the measures which we recommend relate only in an incidental manner to the reserved area of insolvency.

Registration of company charges

1.45 The position as regards Part 25 of the Companies Act 2006 is less clear. These provisions, with their predecessors, have been in force since 1961.[76] They require the registration in the Companies Register of certain types of "charge" over the property of a company. That would include, in our view, any charge constituted by a statutory pledge by a company. It follows that a charge of this type would need to be dual-registered in the Register of Statutory Pledges and the Companies Register.

1.46 Whether the provisions about registration of charges created under Scottish law being registered in the Companies Register should be regarded as being about the law of rights in security, and therefore not reserved, or as being (at least in part) about company law, and thus reserved to the UK Parliament, is arguable. This Commission has previously examined the point, and concluded that the position is unclear, but that on balance these provisions are reserved.[77] Any recommendation to deal with the inconvenience of dual registration would on that view be outside competence. We return to this matter in Chapter 36.

Intellectual property

1.47 Intellectual property law is reserved.[78] But the same points can be made here as about company law, which is to say that the law about rights in security relating to IP is not reserved. The measures which we recommend are for the purpose of a new security right over moveable property. Our policy, however, is to make recommendations which can work within the existing registration scheme for certain securities over IP. We discuss this matter in Chapter 22.

Shipping and aviation

1.48 Shipping law[79] and aviation law[80] are also reserved. Ship mortgages are excluded from this project. So for the most part are security rights over aircraft. But we make

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[73] Scotland Act 1998 Sch 5 Part II Head C2.
[74] See para 1.25 above.
[75] While in this Report we make a small number of recommendations on reserved matters which would require legislation by the UK Parliament, our draft Bill could be taken forward by the Scottish Parliament.
[76] They were introduced (from English law) by the Companies (Floating Charges) (Scotland) Act 1961. Over the years there have been numerous changes. The latest and most important came into force on 1 April 2013.
[77] Scottish Law Commission, Report on Registration of Rights in Security by Companies (Scot Law Com No 197, 2004), Part 6. This relates to the immediate predecessor of Part 25 of the Companies Act 2006, namely Part XII of the Companies Act 1985, but this difference is immaterial.
[78] Scotland Act 1998, Sch 5 Part II Head C4.
[79] Scotland Act 1998, Sch 5 Part II Head E3.

recommendations here[81] about purely Scottish aspects. Any legislation to give effect to these recommendations would therefore have to be effected by the UK Parliament. But this is not an integral part of the new scheme, and so if no Westminster legislation were to be enacted, the Scottish Parliament could still go ahead with the main scheme.

Financial markets

1.49 Regulation of financial markets is reserved.[82] Our recommendations affect the assignation of claims in respect of financial collateral, and the creation and realisation of security over financial instruments as a form of moveable property, including in the making of financial collateral arrangements.[83]

1.50 We consider that assignations and security rights of this type, including financial collateral arrangements, do not relate except in an incidental manner to the subject matter of any financial reservation. In saying this, we have regard in particular to the lack of any effect on the operation of any market as a financial market. We do recommend that in some cases a purchaser in a market will take a financial instrument free from any statutory pledge, but again this limitation on the effect of the statutory pledge for the purposes of acquirer protection would not in our view be outside competence.

1.51 Section 255 of the Banking Act 2009, once commenced, will confer on the Treasury power to legislate, by statutory instrument, on the subject of "financial collateral arrangements". But no change was made to the Scotland Act 1998, so that the Scottish Parliament's legislative competence in relation to that area of law was not altered.[84]

1.52 Section 104 of the Scotland Act 1998 states that "subordinate legislation may make such provision as the person making the legislation considers necessary or expedient in consequence of any provision made by or under any Act of the Scottish Parliament…". Section 104 orders are made by the Secretary of State from time to time, and it is not impossible that legislation emerging from the Scottish Parliament following this Report might be supplemented by a section 104 order in the UK Parliament.

Human rights

1.53 We do not consider that our recommendations raise any human rights issues. We believe that they would be compatible with the European Convention on Human Rights.

EU law

1.54 Following the formal notice of intention to leave the EU made by the UK in March 2017, legislation is to be passed by the UK Parliament to incorporate much of EU law into UK law.[85] In the future that law may be amended or repealed by the UK Parliament or

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[80] Scotland Act 1998 Sch 5 Part II Head E4.
[81] See Chapter 21 below.
[82] Scotland Act 1998 Sch 5 Part II Head A4.
[83] See para 1.54 below.
[84] On financial collateral arrangements see further para 1.54 below.
[85] The European Union (Withdrawal) Bill is at the time of writing undertaking its Parliamentary passage. Other Bills are to follow.

perhaps in some cases the Scottish Parliament.[86] In Chapters 14 and 37 we consider the impact of the Directive on Financial Collateral Arrangements (2002/47/EC). This was implemented in the UK by regulations and we proceed on the basis, notwithstanding the pending exit of the UK from the EU, that the draft Bill requires to comply with these regulations.

Business and Regulatory Impact Assessment (BRIA)

1.55 In line with the Scottish Government's requirements for regulatory impact assessments of proposed legislation,[87] we have prepared a BRIA in relation to our recommendations, which is published on our website. The main points are:

- Scottish moveable transactions law is widely considered to be out of date, inflexible and inadequate.
- Competing jurisdictions, in particular England and Wales, have moveable transactions laws which are more commercially friendly than is the case in Scotland.
- There is significant support for reform and modernisation of Scottish moveable transactions law amongst those who use it. The benefits would be very wide-ranging.
- If implemented, our recommendations for reform would make various types of commercial transactions more efficient, less expensive and less complicated than they currently are. This would lead to greater access to finance for individuals and businesses in Scotland.
- The recommendations would also clarify the existing law, encouraging people and businesses in Scotland to use Scottish law with confidence.

1.56 As all Bills introduced in the Scottish Parliament require an accompanying BRIA there is likely to be a need to update our version when a Moveable Transactions (Scotland) Bill is brought forward. It will be examined as part of the Parliamentary process, especially at Stage 1. We would encourage all those who may be affected by the reforms, or otherwise with an interest in them, to consider engaging with that process at the appropriate time in the future. The task of assessing the likely impact of reform such as the present one, which in large part aims to keep the law up to date and in line with modern demands and commercial expectations, is as crucial as assessing any other legislative or regulatory proposal.

Acknowledgements

1.57 We are grateful to all our consultees and others who have assisted us in various ways, whose names are given in Volume 2. Also listed there is the membership of our advisory group, which we significantly extended as we worked on the draft Bill and this Report. During the course of 2014 to 2017 we had a series of meetings with the advisory

[86] For discussion in a Scottish context see A Page, "Brexit, the Repatriation of Competences and the Future of the Union" 2017 Juridical Review 39 and N Burrows and M Fletcher, "Brexit as Constitutional 'Shock' and its Threat to the Devolution Settlement: Reform or Bust" 2017 Juridical Review 49.

[87] See https://beta.gov.scot/policies/supporting-business/business-regulation/.

group at which we discussed difficult areas of policy and reviewed draft Bill provisions. These meetings and advice given to us at other times by advisory group members, many of whom are practitioners working day by day on moveable transactions, was invaluable. We are grateful to Dr John MacLeod, who assisted us in relation to registration aspects. Significant help was received too from Martin Corbett and his colleagues at Registers of Scotland. We thank also our former Chairman, Lord Drummond Young and former lead Commissioner Professor George Gretton for joining the advisory group and continuing to give us their expertise following their departure from the Commission.

Chapter 2 Outline of the scheme for reform of the law of assignation of claims

Introduction

2.1 This chapter provides an outline of the scheme which we recommend for reform of the law of assignation of claims. The Discussion Paper did the same for the provisional scheme for reform of moveable transactions law.[1] We understand that this was helpful to consultees. As mentioned in Chapter 3 below there was significant support in principle for that scheme. Hence what follows here is broadly similar. It should also be appreciated that the following does not attempt to address all the numerous points of detail discussed elsewhere in this Report.

The scheme in practice

2.2 The difficulties caused by the restrictive nature of the current law are set out in Chapter 3. These affect numerous commercial transactions involving assignation of claims, including (1) notification invoice financing; (2) non-notification invoicing; (3) project finance; (4) assignation of rents; and (5) securitisations. The introduction of the scheme which we recommend would free business from these restrictions and ease the ability to access finance. In the words of one law firm: "the increased efficiencies of the new regime seem bound to decrease transaction costs and likely to increase availability of funding from those slightly deterred by the current Scottish legal uncertainties and inefficiencies."[2]

Claims

2.3 For the purposes of the scheme, a claim would be defined as the right to the performance of an obligation. Typically this would be the right to be paid money. Monetary claims relating to land such as rents would be included.

Completion of title

2.4 Assignation of claims would be completed *either* by intimation to the debtor/account party (as now) *or* by registration in the new Register of Assignations ("RoA"). This reform would significantly assist the invoice financing sector in Scotland because the registration option would allow the effective assignation of claims which have yet to come into existence where intimation is thus not possible.

2.5 Here are some examples. (i) W owes money to X. X can assign this to Y, Y's title being completed by registration, without intimation to W. Y can later assign to Z, this

[1] See Discussion Paper, Chapter 3.
[2] Shepherd and Wedderburn LLP in response to the consultation on the draft Moveable Transactions (Scotland) Bill of July 2017.

assignation being completed by intimation. Thus in a chain of assignations, different methods of completion could be used. (ii) W owes money to X. X fraudulently assigns to Y and also to Z. Y completes title by intimation and Z by registration. Whichever completes title first would prevail.

Intimation

2.6 Intimation could be made in person, by post or courier, or electronically. Either the assignor or the assignee or a representative could do this. It would not be necessary to include a copy of the assignation. The Transmission of Moveable Property (Scotland) Act 1862, which does not meet the needs of modern commerce, would be repealed. It would be made clear that an instruction by the assignee for the debtor to continue to perform to the assignor would not invalidate the assignation. This issue is particularly important in practice in relation to assignations in security.

Register of Assignations

2.7 The RoA would be comparable, in broad terms, with the registers used under UCC–9 and the PPSAs. The main difference would be that the assignation document would be registered.

2.8 We envisage that the RoA would be principally used by banks and other institutions which provide finance in return for the assignation of claims, for example invoices and income streams such as rents and IP royalties. Registration would protect the assignee in the event of the assignor's insolvency, whereas under the current law such protection can only be achieved by intimation.

2.9 The RoA would be a public register. Registration and searching would be completed online. It would, in general, be automated and require minimum human intervention by registers staff.

2.10 The new register would be added to the stable of registers administered by the Keeper of the Registers of Scotland in the Department of the Registers[3] and on the same self-financing basis as most other registers, such as the Companies Register and the Land Register. The costs of the register would be covered by fees for registration, for searches etc. Thus there should be no cost to the taxpayer.

2.11 Registration would be by the name of the assignor. The rules would be fairly demanding as to the identity of the assignor. For companies, not only company name and registered office address would be required, but also company number, because whereas names and addresses can change, the company number stays the same. For natural persons, we recommend that date of birth should be required as well as name and address.

2.12 Where an entry in the register for an assignation contained a seriously misleading inaccuracy, for example the wrong name was given for the assignor, the registration would be ineffective.

[3] Such as the Land Register, the Register of Sasines, the Register of Inhibitions and Adjudications, the Books of Council and Session, etc.

2.13 Registration would have third-party effect. But there would be defined exceptions where a third party would be unaffected. For example, W (the account debtor) owes money to X and X (the assignor) assigns the claim to Y (the assignee). Y completes title by registration. W, unaware of the assignation, pays X. W would be discharged.

2.14 It would be possible for inaccurate entries in the RoA to be corrected. The Keeper, for example, could remove entries which resulted from frivolous or vexatious registrations.

2.15 There would be limited information duties owed to certain persons in relation to assignations which had been registered. For example, a third party with a right to execute diligence against a claim could check whether it had been assigned, if this was not clear from the face of the RoA.

2.16 Registration would not be required for assignations of financial collateral which constituted a security financial collateral arrangement or a title transfer financial collateral arrangement within the meaning of the Financial Collateral Arrangements (No. 2) Regulations 2003.[4]

Assignation of claims not yet in existence

2.17 An assignation of a claim which did not exist when the assignation was registered would not be effective until the claim was acquired by the assignor. It is currently not possible to assign these types of claim, as the assignee cannot intimate to an as-yet non-existent debtor. But private individuals would be unable to assign rights to their salary and similar payments.

Assignation subject to condition

2.18 It would be made clear that an assignation can be made subject to a condition which requires to be satisfied before the assignation transfers the claim.

Anti-assignation clauses

2.19 The law would remain as it is, namely that such a clause would invalidate a purported assignation. But this would be subject to any other statutory provisions, such as sections 1 and 2 of the Small Business, Enterprise and Employment Act 2015.[5]

Protecting the account debtor

2.20 As mentioned above,[6] in an assignation, a debtor who acted in reasonable ignorance of an assignation (for example by paying the previous creditor) would be protected. The debtor would not be deemed to know the contents of the new register.

2.21 The assignee would be subject to information duties, so as to ensure that the debtor was not put in a difficult position. For example, where intimation was by the assignee (who may be unknown to the debtor), evidence of the assignation could be demanded.

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[4] SI 2003/3226.
[5] Sections 1 and 2 of the 2015 Act allow regulations to be made which would render bans on assignation in certain contracts ineffective. See para 13.10 below.
[6] See para 2.13 above.

Assignation in security

2.22 Assignation in security of a claim would continue to be competent, that is the transfer of a claim to the assignee, the latter to hold for the purpose of security. Such assignations would, like other assignations, be completed by intimation or by registration.

Some other issues about assignation

2.23 The rule that an assignee may sue in the assignor's name would be abolished.

2.24 The rule that a mandate can constitute an assignation would be abolished.

2.25 The assignation of a secured claim would carry the security too except in so far as otherwise provided in the assignation document, provided that the security was restricted to the claim.

Codification of the law of assignation

2.26 The law of assignation would not be codified. But the possibility of codification in the future would exist.

Chapter 3 The current law and the case for reform

Introduction

3.1 In the Discussion Paper we outlined the current law in relation to outright assignations.[1] While it is unnecessary to restate that in full here, we do consider it essential to give a brief summary of these areas and the shortcomings of the present law which justify reform.

The current law

3.2 Assignation is the method of transferring incorporeal property in Scotland. With the major exception of Dr Ross Anderson's book published in 2008,[2] it is an area which has been relatively under-researched in modern times.[3] "Outright" or "absolute" assignation means assignation not for the purpose of security, but in practice the rules on outright and security assignations are broadly the same.

3.3 The project in general is limited to the assignation of incorporeal moveable property.[4] Thus assignations of leases are not within its scope. It is furthermore restricted to the assignation of claims (personal rights), in other words rights to the performance of an obligation by another person.[5] Normally that obligation will be to pay money. For example, Jane sells goods to Lauren. Jane's right to be paid for the goods amounts to a claim against Lauren and Jane could transfer that claim to a third party, Kevin.

3.4 What the project does not cover is assignation of other types of incorporeal moveable property, such as corporate shares and bonds, negotiable instruments and intellectual property. Here transfer is normally regulated by specialist legislation,[6] which operates on a UK-basis. In contrast, the transfer of claims is for the most part regulated by the common law.[7]

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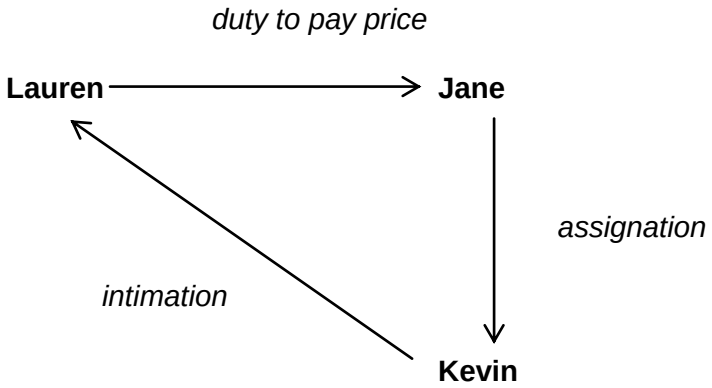
[1] Discussion Paper, Chapter 4.
[2] Anderson, *Assignation*. Dr Anderson was a member of our advisory group.
[3] But see also W A Wilson, *The Scottish Law of Debt* (2nd edn, 1991) ch 27; P Nienaber and G Gretton, "Assignation/Cession" in R Zimmermann, D Visser and K Reid (eds), *Mixed Legal Systems in Comparative Perspective: Property and Obligations in Scotland and South Africa* (2004) 787–818; W W McBryde, *The Law of Contract in Scotland* (3rd edn, 2007) ch 12; and R B Wood in Ruddy, Mills and Davidson, *Salinger on Factoring* paras 7.39–7.73.
[4] But see paras 4.10–4.11 below.
[5] That is to say the correlative of a claim is an obligation, or in Hohfeldian terms, a duty. See further W N Hohfeld, *Fundamental Legal Conceptions as Applied in Judicial Reasoning* (1919). See also Scottish Law Commission, Review of Contract Law: Report on Third Party Rights (Scot Law Com No 245, 2016) paras 3.11–3.13.
[6] Eg the Stock Transfer Act 1963, the Bills of Exchange Act 1882 and the Copyright, Designs and Patents Act 1988.
[7] The main exception is the Transmission of Moveable Property (Scotland) Act 1862, of which we recommend the repeal. See paras 5.29–5.37 below.

3.5 In the assignation of a claim, the transferor (Jane in the above example) is known as the "assignor" or "cedent". The transferee (Kevin) is known as the "assignee" or "cessionary". The debtor (Lauren) is sometimes also known as the "account debtor" or "account party". This is because the assignor is also often a debtor to the assignee (such as in a security assignation) and it is convenient to have a term that distinguishes the debtor in the assigned right.

3.6 In the same way as transfers of land are often preceded by a contract of sale (missives), assignations often give effect to a contract to assign. In terms of the Requirements of Writing (Scotland) Act 1995 writing is neither required for the contract to assign nor the assignation itself. Where writing is used, as is invariably the case in practice, no special words are required,[8] but it must be clear that the grantor of the document intends to assign. The standard wording is "I/We do hereby assign."

3.7 There are normally three stages in the assignation of a claim. First, there is the contract to assign. Secondly, there is the act of assignation, which is typically a formal document. These first two steps are often in practice combined. Thirdly, there is intimation (notification) to the account debtor. It is this final step which actually transfers the claim, in the same way as land is only transferred on registration of the deed of transfer in the Land Register.[9] In the example above, the right to be paid the price is only transferred to Kevin on intimation being made to Lauren.[10] A diagram may assist:



3.8 Intimation is a longstanding feature of Scottish law. Thus, here is Viscount Stair, writing in the seventeenth century: "The assignation itself is not a valid complete right, till it be orderly intimated to the debtor".[11] Hence, it is intimation by means of which the assignee "completes title" to the claim.[12]

3.9 Prior to the passing of the Transmission of Moveable Property (Scotland) Act 1862, normally the only form of intimation was notarial intimation, which required the involvement

[8] See eg *Laurie v Ogilvy* 6 Feb 1810, FC; *Carter v McIntosh* (1862) 24 D 925; *Brownlee v Robb* 1907 SC 1302.
[9] LR(S)A 2012 s 50(2).
[10] In the diagram intimation is made by the assignee, Kevin. As we note in para 3.10, it is also probably competent for the assignor to intimate.
[11] Stair 3.1.6.
[12] See eg *Bank of Scotland Cashflow Finance v Heritage International Transport Ltd* 2003 SLT (Sh Ct) 107.

of five people.[13] The 1862 Act introduced a less cumbersome form of notarial intimation and the following non-notarial method:

> "An assignation shall be validly intimated . . . by the holder of such assignation, or any person authorized by him, transmitting a copy thereof certified as correct by post to such person."[14]

As can be seen, this method requires delivery of a copy of the assignation.

3.10 We understand that nowadays both common law and notarial intimation are rare. The postal method introduced by the 1862 Act is widely used, but not universally. For example, although notice is given by post, a copy of the assignation is not sent. Whether this is an acceptable form of intimation given the pre-1862 stringencies of the common law is unclear. In *Christie Owen & Davies plc v Campbell*[15] the view was stated by the Inner House of the Court of Session that to intimate is simply to inform and that therefore it was unnecessary to use one of the two forms of notarial intimation or the postal method authorised by the 1862 Act. But most of what was said was not essential to decide the case and there was no competing claimant. Thus what is necessary to achieve a valid intimation is unclear. A further point is that while intimation is normally made by the assignee, it is also probably competent for the assignor to intimate, although the law here is also not free from doubt.[16]

3.11 A particularly difficult area in the current law is the assignation of claims which are not yet in existence. For example, a company may wish to raise finance by selling to a finance company the sums due under its future invoices to customers. Thus the claims to be paid the sums would be transferred to the finance company by assignation. But here there is a problem. The identity of future customers may not be known and thus there cannot be intimation to such individuals. Without intimation, there cannot be an assignation.

3.12 Even the doctrine of accretion cannot assist in such cases, although it might help if the identity of the customer can be guessed and there is intimation to him or her following the assignation, but before the claim comes into existence. Accretion of title is a doctrine whereby if X ostensibly conveys to Y a right that X does not have, but X later acquires that right, the right will, at that stage, pass immediately and automatically and without the need for any further act of transfer, from X to Y.[17]

3.13 A fundamental rule of the law of assignation is generally referred to by the Latin tag *assignatus utitur jure auctoris* (the assignee takes the right of the assignor).[18] Thus defences available by the account debtor against the assignor can also be pled against the assignee. For example, Gwyneth owes Henry £1,000 but Henry owes Gwyneth £250. Gwyneth would be entitled to plead the defence known as compensation and set off the £250, so that she

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[13] A procurator (lawyer) acting on behalf of the assignee, a notary public, two witnesses and the debtor. See Anderson, *Assignation* para 6-23.
[14] 1862 Act s 2.
[15] [2009] CSIH 26, 2009 SC 436. And in the Outer House decision of *Promontoria (Ram) Ltd v Moore* [2017] CSOH 88 at para 96 Lord Bannatyne stated that the 1862 Act is "permissive not prescriptive" but without further discussion.
[16] See Anderson, *Assignation* para 6-30.
[17] See *Buchanan v Alba Diagnostics Ltd* 2004 SC (HL) 9, discussed in R G Anderson, "*Buchanan v Alba Diagnostics*: Accretion of Title and Assignation of Future Patents" (2005) 9 EdinLR 457.
[18] See Anderson, *Assignation* ch 8.

only pays Henry £750. Imagine that Henry assigns the £1,000 claim against Gwyneth to Isabel. Gwyneth is still entitled to exercise her right of compensation and only pay Isabel £750. (Provided that the claim for £250 arose before the £1,000 claim was transferred).

3.14 Not all claims can be assigned. For example, the assignation of the right to social security payments is forbidden by statute,[19] as is the assignation of pension rights.[20] Further, the parties to a contract which gives rise to the claim may agree that it cannot be assigned. This is known as an "anti-assignation clause" (or in England, "non-assignment clause"). The Scottish and English courts have both upheld the validity of such clauses.[21] Nevertheless, very recent Westminster legislation allows the Scottish Ministers to declare these invalid in relation to trade receivables.[22]

3.15 It is competent but uncommon to assign part only of a claim. So if Alan owes Beth £100,000, she could assign £60,000 to Charles and the balance she could retain, or could assign it to Dora. But the exact rules are underdeveloped, in particular as to where partial assignation is incompetent.[23] Another area which suffers from a lack of clarity is assignations subject to a suspensive condition, that is to say an assignation which is not to take effect until a future event happens. There is little authority on this matter.[24] There are also uncertainties in relation to the circumstances in which a mandate can operate as an assignation.[25]

The case for reform

3.16 Without a doubt, the part of the law of assignation of claims which is regarded as most unsatisfactory, as well as outmoded and inflexible, is intimation.[26] Most other legal systems do not require intimation as a pre-requisite for transfer.[27] The need for intimation in Scotland is particularly detrimental as regards the invoice discounting sector, which wishes to have the ability to assign claims which do not yet exist.[28] More generally, it is very cumbersome to have to intimate to hundreds if not thousands of separate customers of a business that their invoices have been assigned. The result is that workarounds need to be used, in particular to protect against the risk of the assignor becoming insolvent prior to intimation. One is to write contracts under English law, so that an equitable assignment (which does not require intimation) can be used. This increases the transaction costs of Scottish-based parties, who otherwise would want to use Scottish law. Further, it is not entirely clear following the case of *Joint Administrators of Rangers Football Club Plc, Noters*,[29] which involved the sale of receipts from future season tickets, that the use of

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[19] Social Security Administration Act 1992 s 187.
[20] Pensions Act 1995 s 91.
[21] *James Scott Ltd v Apollo Engineering Ltd* 2000 SC 228; *Linden Gardens Trust Ltd v Lenesta Sludge Disposal Ltd* [1994] 1 AC 85.
[22] Small Business, Enterprise and Employment Act 2015 ss 1 and 2. See paras 13.2–13.11 below.
[23] See Anderson, *Assignation* para 2-22 to 2-24.
[24] But see Anderson, *Assignation* paras 10-55 to 10-66.
[25] In other words where A mandates (authorises) B to collect a claim. See Discussion Paper, paras 4.46-4.50.
[26] For a valuable recent account in response to the Discussion Paper, see A McAlpine, "Raising finance over claims to payment and reform to the law of outright assignation" 2015 Juridical Review 275.
[27] See Discussion Paper, Appendix B. See also R G Anderson and J W A Biemans, "Reform of Assignation in Security: Lessons from the Netherlands" (2012) 16 EdinLR 24 at 28.
[28] On the benefits of factoring to businesses, see I Istuk, "The potential of factoring for improving SME access to finance" in F Dahan (ed), *Secured Financing in Commercial Transactions* (2016) 212–234.
[29] [2012] CSOH 55, 2012 SLT 599. See para 15.28 below. See also G L Gretton, "The Laws of the Game" (2012) 16 EdinLR 414 and Lord Reed, "Triremes and Steamships: Scholars, Judges, and the Use of the Past",

English law in such circumstances is effective.[30] Another workaround is to use trust structures,[31] although these too are vulnerable to the problems identified in the *Rangers* case.[32] Moreover, the use of trusts in debt financing transactions principally rests on the authority of one decision of the Inner House of the Court of Session from 1987[33] and a decision of the same court a few years before in 1981 expressed deep concern about the use of trusts in the context of security transactions.[34]

3.17 A further difficulty with intimation, identified above, is that it is not clear exactly what is needed for a valid intimation. Parties to transactions require as much certainty as possible and then current law does not give them this. As we have seen, there is uncertainty in areas other than intimation. Assignations subject to suspensive conditions play an important role in certain commercial transactions[35] but the lack of clear legal authority in relation to these has, we understand, led to disputes in relation to what the law actually is. Other areas where the law is unclear, as mentioned earlier, include the operation of mandates as assignations, and partial assignation.

3.18 Reform is also justified by the current structure of the law of assignation of claims not being user-friendly. The law is a mix of common law (including the institutional writings of the late seventeenth to the early nineteenth centuries, such as those of Viscount Stair, and case law often dating from before 1900) and the Transmission of Moveable Property (Scotland) Act 1862. There is a considerable amount to be said for placing the key rules in modern statutory form. Providing a clear legal framework would be a considerable benefit to business. Moreover, the existing law developed in social and commercial conditions very different from those now prevailing, hence its unsatisfactory state in certain areas.

Previous attempts at reform

3.19 Unlike our law on security over moveables, the law on assignation as such has not hitherto been reviewed. But the Crowther Report,[36] the Diamond Report[37] and the Halliday Report[38] recommended the adoption of a UCC–9/PPSA-type system.[39] Under such a system the rule is that in certain types of case an assignment (the equivalent of an assignation), even where not for the purposes of security, must be the subject of a registered financing

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The Scrymgeour Lecture, University of Dundee, 30 October 2015, pp 9–10, available at https://www.supremecourt.uk/docs/speech-151030.pdf.

[30] See R B Wood in Ruddy, Mills and Davidson, *Salinger on Factoring* paras 7.40–7.44.

[31] See Scottish Law Commission, Report on Trust Law (Scot Law Com No 239, 2014) paras 2.13–2.15.

[32] See Lord Hodge, "Does Scotland need its own Commercial Law?" (2015) 19 EdinLR 299 at 307. See also *Akers (and others) v Samba Financial Group* [2017] UKSC 7 at paras 36 to 37 per Lord Mance.

[33] *Tay Valley Joinery Ltd v C F Financial Services Ltd* 1987 SLT 207. See K G C Reid, "Trusts and Floating Charges" 1987 SLT (News) 113; G L Gretton, "Using Trusts as Commercial Securities" (1988) 33 JLSS 53; D P Sellar, "Trusts and Liquidators" 1989 SLT (News) 143 and W A Wilson and A G M Duncan, *Trusts, Trustees and Executors* (2nd edn, 1995) ch 4.

[34] See *Clark Taylor & Co Ltd v Quality Site Development (Edinburgh) Ltd* 1981 SC 111 at 116 per Lord President Emslie: "if a condition . . . designed only to freeze assets of a debtor and to keep them out of other creditor's hands until a particular creditor's debt is paid in full, were to be regarded as constituting a proper trust in accordance with the law of Scotland, and were to be adopted widely by sellers of goods, the damage which would be done to the objectives of the law of bankruptcy and liquidation would be incalculable."

[35] For example, in receivables financing where conditions for the purchase of the receivables have to be satisfied before the assignation is to take effect.

[36] Report of the Committee on Consumer Credit (Cmnd 1017, 1960).

[37] A L Diamond, A Review of Security Interests in Property (Department of Trade and Industry, 1989).

[38] Report by the Working Party on Security over Moveable Property (1986) (available on the SLC website).

[39] See Chapter 18 below.

statement in order to be effective against third parties. In the Discussion Paper we discussed whether a UCC–9/PPSA-type system should be introduced in Scotland.[40] Our view was that it should not be.

Consultation

3.20 Our consultees also opposed the UCC–9/PPSA approach.[41] In Chapter 3 of the Discussion Paper we set out our alternative proposed new scheme for reform of moveable transactions law which was similar to the final version of the scheme now set out in Chapters 2 and 16 of this Report. We asked whether such a scheme would be appropriate. To this question, we received a considerable number of thoughtful responses.

3.21 The vast majority of consultees expressed strong support in principle. Thus the Asset Based Finance Association (ABFA) stated:

> "Invoice finance is becoming one of the most necessary routes to finance for businesses in the UK, whether Scottish or anything else. We feel that the capacity of the Scottish legal system to deal with what is required to enable the offering of invoice finance to Scottish businesses has not kept pace with the developments in other western European legal systems, far less than with English law which has always offered a benign environment for this. This is a reform whose time not only has come but, in fact, came a long time ago and is very much needed."

3.22 It also commented:

> "We see the provisional proposals in the Discussion Paper as, for the first time, giving our members a real basis to work confidently within Scots law."

3.23 CBI Scotland said:

> "We welcome the proposals in the Paper and wish to endorse what we see as an overdue reform of the law, which will improve our members' access to credit in Scotland. We consider that Scots law at present puts difficulties in the path of banks and finance companies offering credit facilities to businesses based in Scotland and, while ways round that have been devised over the years - usually involving the use of English law and the submission to the jurisdiction of the English courts - this has not been a panacea and difficulties remain. This can be more challenging for SMEs than for major corporates, the latter having greater ease of organising their credit lines furth of Scotland than SMEs may do. To put it another way, while we have no mandate for stating that Scots law and English law should be the subject of wholesale harmonisation, it is detrimental to Scottish SMEs competing in what is now a UK-wide market, if not a wider one, to find that their ease of accessing credit is constrained in a way which would not be the case if they were English based."

3.24 The Committee of Scottish Clearing Bankers (CSCB) stated:

> "The CSCB welcomes the principle of reform of the law in this area as it will benefit businesses in Scotland."

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[40] Discussion Paper, Chapter 21.
[41] See further Chapter 18 below.

3.25 The Federation of Small Businesses commented: "From reading your recommendation it does look like this area of Scots Law could well benefit from review from the point of view of the business community." We subsequently met twice with Colin Borland, its Head of External Affairs, Devolved Nations as we worked on this Report. He made the following statement on our scheme for assignation:

> "A lack of cash is fatal to a business – and too much of it is tied up in unpaid invoices. We calculate that 3,500 businesses go bust in Scotland every year while waiting to be paid for work they've already done. Using the sort of simple process proposed to make it easier to assign claims will help smaller firms get cash into the business while perhaps encouraging new players to enter the finance market in Scotland."

3.26 ICAS/R3[42] said: "In principle both organisations are broadly in favour of the proposals considering them to be business friendly."

3.27 The Scottish Council for Development and Industry stated:

> "SCDI has received input from members on the Discussion document. We were especially interested to note that a number of proposals have been made aimed at improving the way in which security over moveables can be created in Scotland. To the extent that such proposals support the more efficient running of commerce or have the effect of encouraging commerce in Scotland (and therefore sustainable economic prosperity) by enabling Scottish-based businesses to raise finance as efficiently as possible, such amendments would be welcomed.
>
> The report usefully highlights certain aspects of Scots law which currently either restrict our ability to effect certain security arrangements equivalent to those elsewhere in the UK and beyond or, are so cumbersome in their requirements as to make their creation impractical. We would support amendments to the law which would have the general effect of removing some of the barriers and restrictions which arguably put businesses in Scotland at a disadvantage."

3.28 As we worked towards completion of this Report we endeavoured to consult other business interests to gauge their views. The scheme was supported by members of ABFA and the Finance and Leasing Association (FLA) who we surveyed.

3.29 The Law Society of Scotland responded to the Discussion Paper and broadly were in favour of the proposed scheme, but had some concerns on points of detail in relation to security rights.[43] When we subsequently consulted on our draft Bill in July 2017 the Society said:

> "We are aware that there is strong support for these changes across the profession and would encourage the Scottish Government to bring forward legislation in this area in line with the Commission's recommendations. The time dedicated by many legal professionals to the Commission's reform project further evidences the importance of the reforms to ensure that the Scottish legal system is fit for purpose and reflects modern commercial realities, in particular in relation to the increasingly electronic nature of communications and commercial transactions. We consider that the Bill as a whole presents a modern, balanced and practical set of reforms that

[42] Institute of Chartered Accountants of Scotland/Association of Business Recovery Professionals.
[43] We address these in Chapter 18 below.

should provide benefits to Scottish businesses – including, and perhaps, especially, SMEs – while protecting consumers."[44]

3.30 In its response to the Discussion Paper the WS Society said:

> "We welcome the Law Commission's Discussion Paper and very much hope that at last some legislative reform will be forthcoming in this area – Scots law is in our view out of kilter with the requirements of the commercial world and the rules in other Western legal systems and reform has been neglected for too long. We applaud the Law Commission's decision to limit its remit in the belief that this may remove controversial issues from the proposals, giving them more chance of enactment."

3.31 There was also support from a number of law firms and practising solicitors. One law firm[45] stated:

> "We believe that the Commission's paper is an excellent starting point in improving Scotland as a commercial jurisdiction."

3.32 Professor Stewart Brymer wrote: "Overall, I would simply like to commend the conclusions of the Discussion Paper. It is time for Scots law to develop in this area."

3.33 When we consulted on an advanced version of our draft Bill in July 2017 there was again strong general support from stakeholders. For example, Dr Hamish Patrick of Shepherd and Wedderburn commented that reform was "very much overdue" and that his firm "very much support[ed] the draft Bill."

3.34 Any broad concerns raised by consultees to the Discussion Paper, for example, the interaction with insolvency law were directed at the part of the scheme dealing with security over moveable property and we deal with these in Chapter 18 below.

[44] See also E Arcari, "Corporate Briefing" (2017) 62 JLSS 29 at 30 which discusses the draft Bill consultation, stating that the Commission "has been working to provide much sought-after reform".
[45] Dundas & Wilson. Now CMS Cameron McKenna Nabarro Olswang.

Chapter 4 Assignation: general

Introduction

4.1 This chapter and the following three chapters address the first strand of the project: outright transfer (assignation) of incorporeal moveable property, in other words transfer of moveable property that does not have a physical presence.

4.2 It is necessary to define the scope more precisely. First, following the Discussion Paper,[1] we do not address the transfer rules for special types of incorporeal moveable property, such as negotiable instruments, company shares and intellectual property. The law governing such property typically has UK-wide application[2] and Scotland-only reforms would not be sensible. Our recommended reforms instead relate to reform of assignations of claims, that is to say rights of one person against another in respect of the performance of an obligation, typically contractual rights to be paid money.

4.3 Secondly, as will be discussed further below, in response to representations from consultees we think it appropriate to cover the assignation of certain claims relating to heritable property (land), in particular assignation of rents, where the current law is also unsatisfactory.

4.4 Thirdly, while for the most part we deal with outright assignation here, our recommendations also apply to assignation in security. For example, a debtor might assign sums owing to it in security to a creditor. The sums would be used by the creditor to pay the debt if the debtor defaults. Where there are special issues relating to assignation in security we will highlight them.

4.5 We begin with a general recommendation:

1. There should be legislative reform of the law of assignation of incorporeal moveable property consisting of the right by a person against another person to the performance of an obligation.

Assignor and assignee

4.6 The traditional term for the party granting an assignation in Scottish law is the "cedent".[3] It originates from the same linguistic source as "cession", another word for assignation.[4] Under English influence, the term "assignor" has also come to be used.[5] This

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[1] Discussion Paper, para 14.2.
[2] For example, the Bills of Exchange Act 1882, the Stock Transfer Act 1963 and the Copyright, Designs and Patents Act 1988.
[3] See, for example, Stair 3.1.4; Anderson, *Assignation* para 1-02 and R G Anderson and J W A Biemans, "Reform of Assignation in Security: Lessons from the Netherlands" (2012) 16 EdinLR 24 at 26.
[4] It is the standard term in France and South Africa today. Note also *cessione* in Italian law.
[5] See, for example, P Nienaber and G Gretton, "Assignation/Cession", in R Zimmermann, D Visser and K Reid (eds), *Mixed Legal Systems in Comparative Perspective* (2004) 787 at 788 and *Apollo Engineering Ltd v James Scott Ltd* [2012] CSIH 88 at para 15.

also tends to be the term found in international instruments, such as the DCFR.[6] We consider in addition that this is a more accessible term to the layperson and we therefore use it in the draft Bill. The grantee of an assignation is an "assignee".[7]

4.7 We recommend:

2. The party granting an assignation should be referred to as the "assignor" and the grantee should be referred to as the "assignee".

(Draft Bill, s 1(2)(a) & (b))

Subject matter of assignation: claims

Terminology

4.8 We require also a term for the property that is being transferred by the assignation. As noted above,[8] our scope does not extend to special types of incorporeal moveable property. Rather, we recommend reform in relation to what are conceptually termed "personal rights", in other words the right of one person enforceable against another person to the performance of an obligation. For the reasons set out in Chapter 3 we consider that the law here is unsatisfactory and requires reform.

4.9 For example, Iris owes Joanna £1,000, payable next year. Thus Joanna has a personal (contractual) right against Iris to be paid £1,000. Imagine that Joanna requires money now. She could sell her right against Iris to Kenneth. (This would normally be at a discount, because Kenneth has to wait until next year to be paid.) The way in which the personal right would be transferred would be by *assignation* and under the current law the assignation would be completed by intimation to Iris by Kenneth.[9] Frequently reference is made to "assignation of debts". Thus Joanna can be said to be assigning Iris's debt. But strictly this is incorrect. It is rights which are assigned and not obligations.[10]

4.10 In relation to terminology for our draft Bill there are several options. The first is "incorporeal moveable property", but this can be ruled out as being too wide for the reasons given above.[11] The second is "right", but again this seems too wide.[12] The third is "personal right" but we think that this may cause confusion for the layperson, as it could be viewed as meaning something like a human right to privacy. The fourth is "claim". This is a term which can be used to describe the personal right of one person against another, for example a monetary claim.[13] It has been criticised by Professor Eric Clive on the basis that it can also be used to mean the assertion of a right that may be contested by others, such as an

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[6] DCFR III.–5:102(1).
[7] See, for example, Stair 3.1.4; Anderson, *Assignation* para 1-02. But sometimes the term "cessionary" is used, particularly in older texts. Thus Balfour, *Practicks* 169 (Stair Society vol 21, (1962) edited by P G B McNeill) refers (in Scots) to "cessioner".
[8] See para 4.2 above.
[9] Joanna could intimate rather than Kenneth, but normally it is the assignee who intimates.
[10] Discussion Paper, para 4.15.
[11] See para 4.2 above.
[12] Cf DCFR Book III chapter 5.
[13] Anderson, *Assignation* para 1-02; R G Anderson and J Biemans, "Reform of Assignation in Security: Lessons from the Netherlands" (2012) 16 EdinLR 24 at 26. It also fits with Hohfeldian terminology.

insurance claim or a damages claim.[14] Nevertheless it has the advantages of brevity and of being narrower than "right". It is also familiar internationally[15] and has a good historical pedigree in Scotland.[16] It is the term which we use in the draft Bill.

4.11 We recommend:

3. The subject matter of the assignation should be referred to as a "claim".

(Draft Bill, s 1(1))

Definition of "claim"

4.12 It is also necessary to define "claim" more particularly. In general terms, it is the right to the performance of an obligation, typically an obligation to pay money.[17] It therefore does not include special forms of incorporeal moveable property, such as intellectual property. A patent is not the right to the performance of an obligation.

4.13 Our original intention was that the scope of our recommended reforms would be limited to claims which are "moveable", in other words in essence do not relate to land. While Scottish property law is ultimately unitary in nature,[18] there is of course a well-established distinction between heritable (immoveable) and moveable property. A project on moveable transactions concerns the latter and not the former.[19] On consultation, however, we received strong support for reform of the law in relation to assignation of rents. In practice, it is common for lenders to take an assignation in security of rents from borrowers who are the landlords of commercial premises, perhaps of a shopping centre with multiple units. It is cumbersome and expensive to have to intimate the assignation to the tenants of all the units. As Dr Hamish Patrick has noted:

> "Assignation of rents [presents] very similar issues in practice to assignation of book debts, particularly for large portfolios of leased properties where there is a frequent turnover of leases in the period during which a fixed security is to operate."[20]

4.14 We have considered these representations from consultees. We have concluded that the assignation of rents is little different from the assignation of the right to any other sums and that there would be great practical benefit in widening the scope of our recommended reforms to include these. In particular, we note that it is not competent for an assignation of rents to be registered in the Land Register.[21] In fact only leases of land exceeding twenty years can be registered there.[22] Short leases (twenty years or less)

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[14] See E Clive, "The Assignment Provisions of the Draft Common Frame of Reference" 2010 Juridical Review 275 at 277. Such claims, however, can be viewed as illiquid claims and are similarly capable of assignation.
[15] See eg the Rome I Regulation, discussed in Chapter 15 below.
[16] See Hume, *Lectures* III,1.
[17] Less usually, it will be the right to the performance of a non-monetary obligation, under which the debtor is obliged to do or not to do something.
[18] Reid, *Property* para 1.
[19] Although in the Discussion Paper we did propose one reform relating to standard securities. See paras 13.34–13.35 below.
[20] H Patrick, "A View from Practice" (2012) 16 Edin LR 272 at 277.
[21] See LR(S)A 2012 s 49 as to what is registrable. Dr Patrick (see previous footnote) moots registration in the Land Register as a possibility but we think that registration in the RoA would be more suitable, not least because only long leases can be registered in the Land Register.
[22] Registration of Leases (Scotland) Act 1857 s 1.

cannot. Therefore our recommendation below, which would allow assignations of claims to be registered in the new Register of Assignations, would not lead to an untidy overlap with the land registration law. We consider, however, that only monetary rights relating to land should fall within the definition of "claim". Allowing assignation of non-monetary rights relating to land to be registered in a register dealing primarily with moveable property seems a step too far. We think that these should be excluded. Ultimately whether a right relates to land has to be determined on a case by case basis. There is a statutory precedent in the Prescription and Limitation (Scotland) Act 1973, under which obligations relating to land are subject to the long negative prescription.[23] A lease of land itself would not fall within the definition of a claim because a lease is not the right to the performance of an obligation.

4.15 Rights under negotiable instruments are rights to the performance of obligations, but as negotiable instruments are a special area of the law, our reforms to the law of assignation should not apply to them.

4.16 We therefore recommend:

4. "Claim" should be defined as:

(a) a right to the performance of an obligation; but

(b) excluding a non-monetary right relating to land or a negotiable instrument.

(Draft Bill, s 42(2))

Debtor

4.17 In the example above,[24] Iris owed Joanna £1,000 and Joanna assigned her claim against Iris to Kenneth. Joanna is the assignor and Kenneth is the assignee. It is also necessary to have a term for Iris. She could be referred to as the "account debtor" or "account party". These terms are used for precision as an assignation might be in security and in such a transaction there are two debtors: (a) the assignor who is granting the assignation in security of a debt; and (b) the debtor against whom the claim being assigned is enforceable. But we consider it possible for the draft Bill simply to use the term "debtor" as the obligant in the claim.[25] This is because the term "assignor" is used to denote the granter of the assignation, albeit in the circumstances of the transaction as a whole that person is also a debtor.

4.18 We recommend:

5. The party against whom the claim is enforceable should be referred to as the "debtor".

(Draft Bill, s 1(2)(c))

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[23] Prescription and Limitation (Scotland) Act 1973, Sch 1 para 2(e). For discussion, see D Johnston, *Prescription and Limitation* (2nd edn, 2012) paras 6.54–6.62.
[24] See para 4.9 above.
[25] As is the case in the DCFR Book III chapter 5.

Writing

4.19 An assignation will often be preceded by a contract to assign. This is typical of the contract/conveyance distinction recognised by property law.[26] Thus in the transfer of land there will be a contract of sale, known as missives, followed by the actual conveyance, known as a disposition. Before the Requirements of Writing (Scotland) Act 1995, the law was that writing was not required for the contract to assign a claim, but was required for the assignation itself.[27] In other words a contract to assign could be entered into orally, but an assignation had to be signed by the assignor. The 1995 Act,[28] implementing a 1988 Report of this Commission,[29] provided that assignations no longer had to be in writing. In the Discussion Paper we expressed the view that with the benefit of hindsight, the Report may not have fully considered the issues.[30] Thus the requirement under the current law to intimate (notify) the assignation to the debtor presupposes that there is a written document that can be exhibited. Without writing it will be difficult to satisfy the debtor that the claim has been transferred. But it can be argued in contrast that an assignee who is so foolish as to take an oral assignation must bear the consequences.

4.20 We asked consultees whether they shared our view that agreements to assign should not be subject to any requirement of form. There was unanimous agreement from the consultees who responded to this question.

4.21 Our next question was whether assignations should require to be in writing. If they should, we asked whether they should require to be signed by the granter only, or by both parties. Writing and signature could be electronic as well as paper-and-ink. Consultees were generally supportive of the need for writing. ABFA noted that as far as its members were concerned "assignations will always be in writing, though that writing may be electronic." Dr Ross Anderson wrote: "No formalities need be required for the contract to assign. But the translative agreement – the assignation as transfer – does, I think, require *some* formality." The Faculty of Advocates, noting the issue of information duties owed by the assignee to the debtor,[31] felt that the balance was tilted in favour of requiring writing. It further noted that if reform is to proceed on the basis of offering registration as an alternative to intimation to the debtor in order to complete an assignation,[32] this presupposes the need for writing. We agree.[33]

4.22 As to the matter of who should sign the assignation, most supported signing by the assignor only. David Cabrelli wrote: "As a unilateral act of the cedent, I'm not sure why the

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[26] In German, the *Trennungsprinzip* or *Trennungsgrundsatz.* See eg K Schreiber, "Die Grundprinzipien des Sachenrechts" 2010 Jura 272–275 and M-R McGuire, "National Report on the Transfer of Movables in Germany" in W Faber and B Lurger (eds), *National Reports on the Transfer of Movables in Europe Vol 3: Germany, Greece, Lithuania, Hungary* (2011) 1 at 20.

[27] McBryde, *Contract* para 12.52 and references therein.

[28] Requirements of Writing (Scotland) Act 1995 s 11(3).

[29] Scottish Law Commission, Report on Requirements of Writing (Scot Law Com No 112, 1988) paras 2.51 and 2.52.

[30] Discussion Paper, para 4.29.

[31] See paras 12.17–12.26 below.

[32] See paras 5.1-5.22 below.

[33] More generally, we note that under the reforms to the French Civil Code which came into effect on 1 October 2016 writing is required for assignment. Article 1322 states: "La cession de créance doit être constatée par écrit, à peine de nullité." (The assignment of a claim must be in made in writing on penalty of nullity.") Writing is also required in the Netherlands. See R G Anderson and J W A Biemans, "Reform of Assignation in Security: Lessons from the Netherlands" (2012) 16 EdinLR 24 at 42.

assignee should be required to sign too." Dr Anderson noted: "Although the deed need be subscribed only by the cedent, the assignee must agree. In the ordinary case, acceptance is implicit and evidenced by acceptance of delivery of the deed of assignation." But John MacLeod argued that both assignor and assignee's signatures should be required as transfer is a bilateral act. In contrast, Brodies and the Law Society of Scotland favoured signature by the assignor only on the basis that execution in counterpart (the ability of the parties to sign separate versions of the document) is not recognised in Scotland. This form of execution is now competent by virtue of the Legal Writings (Counterparts and Delivery) (Scotland) Act 2015, based on our Report on Formation of Contract: Execution in Counterpart.[34] Nevertheless, we agree with our consultees that there is not a compelling case to change the position under the current law, whereby only the assignor is required to sign. This mirrors the position for dispositions of land, which only require to be signed by the granter.

4.23 As to the methods of signing, subscription in ink is well-understood. The Requirements of Writing (Scotland) Act 1995 refers to this as execution of a "traditional document".[35] In relation to electronic signature, the 1995 Act describes this as "authentication"[36] and under the relevant regulations made under the Act only an "advanced electronic signature"[37] is permissible. This is a sophisticated type of signature "(a) which is uniquely related to the signatory, (b) which is capable of identifying the signatory, (c) which is created using means that the signatory can maintain under his sole control, and (d) which is linked to data to which it relates in such a manner that any subsequent change of data is detectable".[38] The policy reason is to provide the signature with an appropriate level of evidential value and having the definition in regulations enables future-proofing because these can be more easily changed to take account of technological developments.[39] We consider that electronic signature of assignations should be subject to these provisions, but that the Scottish Ministers should have the power to vary this requirement, if, for example, they consider in the interest of facilitating commerce that a less strict approach is justified. In the interests of further flexibility we think that they should have power to amend the meaning of "execution" in relation to a traditional document.

4.24 We therefore recommend:

6. (a) Agreements to assign claims should not be subject to any requirement of form.

(b) Assignations of claims should require to be in writing signed by the assignor only. Writing and signature may be electronic as well as paper-and-ink under the rules in the Requirements of Writing (Scotland) Act 1995. The Scottish Ministers should have power to modify the rules as regards execution and authentication in relation to assignations.

(Draft Bill, ss 1(1), 118(1) & (5))

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[34] Scot Law Com No 231, 2013.
[35] Requirements of Writing (Scotland) Act 1995 ss 1A and 2.
[36] 1995 Act s 9B(2).
[37] 1995 Act s 9B(1) and the Electronic Documents (Scotland) Regulations 2014 (SSI 2014/83) reg 1(1) and (2).
[38] The definition is from the Electronic Signatures Regulations 2002 (SI 2002/318).
[39] K G C Reid, *Requirements of Writing (Scotland) Act 1995* (2nd edn, 2015) 32–33.

Identification of the claim

4.25 The specificity principle is one of the underpinning principles of property law. To transfer property, or create rights in that property which are good against the world, the property must be properly identified.[40] Like many principles, there are qualifications. For example, a floating charge can be granted over a company's "property and undertaking"[41] ie all its assets without the need for further specification. As the company trades, assets will be sold and new assets acquired. The floating charge attaches on the appointment of a receiver or on the company's liquidation to the property owned by the company at that time.[42]

4.26 Clearly, the assignation document should require to identify the claim, because otherwise the document would be meaningless without it stating what is to be transferred. In commercial practice, however, it is normal to assign multiple claims. For example, a company might assign its customer invoices to an invoice discounter. To require every invoice to be individually described in the assignation document would be cumbersome. Moreover, it would be impossible in the case of future invoices where the supply of goods or services which results in the rendering of the invoice has not yet been carried out. The customer may well be unknown too. To facilitate commerce, it should be made clear in the new legislation that the specific description of a claim is not required in the assignation document. Rather, identification by reference to a particular class, for example "all plumbing invoices" or "all plumbing invoices issued in July 2018" should be permissible.

4.27 Moreover, the claim would not be transferred by the assignation until it becomes identifiable as a claim to which the assignation document relates, in other words a claim which falls within the relevant class. The commentary to the relevant DCFR article[43] on this subject gives the following example:

> "S, a furniture manufacturer, supplies furniture to retail shops and department stores. S agrees to sell to F, a factoring company, such of its existing and future rights to payment as are listed in schedules from time to time sent by S to F. There can be effective assignments as to all rights so listed."[44]

4.28 Thus it is the listing of the rights to payment in the schedules and the sending of these to the factoring company which enables the rights to be transferred. Until then there can be no transfer. A broad parallel can be made with the floating charge. For it to be enforced by receivership or liquidation requires the process of attachment at which point it becomes a fixed security encumbering the specific property held by the company at that time.

4.29 It may be helpful to give some further examples. Example 1. A multi-trade company decides to assign all its current invoices[45] for plumbing jobs to a finance company. As long as an invoice is current and is for plumbing work it will be assigned. Example 2. As well as

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[40] See Gretton and Steven, *Property, Trusts and Succession* paras 4.13–4.15.
[41] Companies Act 1985 s 462(1).
[42] Although ordinarily now floating charges are enforced by administration, where attachment is not automatic but at the option of the administrator. See D Cabrelli, "The curious case of the 'unreal' floating charge" 2005 SLT (News) 127. See also A D J MacPherson, *The Attachment of the Floating Charge in Scots Law* (PhD Thesis, University of Edinburgh, 2017).
[43] DCFR III.–5:106. See also the UNIDROIT Principles of International Contracts (2010) article 9.1.6.
[44] DCFR Commentary, p 1028.
[45] A claim of course can exist without an invoice being issued.

assigning current invoices for plumbing jobs, the assignation document also assigns current invoices for jobs in any other areas "to be agreed by the parties". There is subsequently an agreement to include current invoices for electrical work. These invoices are now assigned. The parties should of course careful records of such agreements and schedules of invoices which are to be assigned in case the assignor subsequently becomes insolvent.

4.30 We recommend:

7. (a) The assignation document should require to identify the claim.

(b) Where an assignation document assigns multiple claims these should not require to be individually identified provided that they are identified as a class.

(c) For a claim to be transferred it should require to be identifiable as a claim to which the assignation document relates.

(Draft Bill, ss 1(3) & (4) and 3(1) & (2)(c))

Partial assignation

4.31 Usually a whole claim will be assigned. So if Alan owes Beth £100,000, Beth could assign the claim to Charles. But it would also be possible for her to assign only £60,000 of the claim to Charles. She could retain the rest, or indeed assign it to Dora.[46]

4.32 Partial assignations can be burdensome to debtors. Instead of having to perform to one person, they have to perform to two or more. In the Discussion Paper[47] we set out the rule in the DCFR:

> "(1) A right to performance of a monetary obligation may be assigned in part.
>
> (2) A right to performance of a non-monetary obligation may be assigned in part only if:
>
> (a) the debtor consents to the assignment; or
>
> (b) the right is divisible and the assignment does not render the obligation significantly more burdensome.
>
> (3) Where a right is assigned in part the assignor is liable to the debtor for any increased costs which the debtor thereby incurs."[48]

4.33 We thought that this was a sound approach, and a natural development of our existing law. We asked consultees whether they agreed that the rule should be adopted. Those who responded were all supportive, but several emphasised that the rule requires to be subject to any express provisions in the agreement giving rise to the claim. We agree. The statutory rule should be a default one. In particular it should be possible for the parties

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[46] See Anderson, *Assignation* paras 2-22 to 2-24. In English law, partial assignment is not competent, except in equity. See *In Re Steel Wing Co Ltd* [1921] 1 Ch 349.
[47] Discussion Paper, para 14.71.
[48] DCFR III.–5:107.

to the claim to exclude assignation in part or to limit its competence.[49] If the claim arises from a unilateral undertaking, that is to say a promise, the promisor too should be able to impose conditions which are different from the default rule. Finally, the debtor and assignor should also be able to depart from the default rule that the assignor is liable to the debtor for additional expense arising out of the assignation being in part.

4.34 We recommend:

8. (a) It should be competent to assign a claim in whole or in part.

(b) But if the claim is not a monetary claim, the claim should only be assignable in part where either:

(i) the debtor consents, or

(ii) the claim –

(a) is divisible, and

(b) assigning it in part does not result in its becoming significantly more burdensome for the debtor.

(c) But these rules should be subject to:

(i) any agreement of the parties to the claim or,

(ii) where the claim arises from a unilateral undertaking, any statement by the person giving the undertaking,

in relation to the extent to which the claim is assignable.

(d) Except in so far as the debtor and the assignor otherwise agree, the assignor should be liable to the debtor for any expense incurred by the debtor because the claim was assigned in part rather than in whole.

(Draft Bill, s 6)

[49] See paras 13.1–13.11 below.

Chapter 5 Assignation: completion of title

Introduction

5.1 Completion of title is probably the single area where there is most dissatisfaction with the current law of assignation of claims. For an assignation to be completed, intimation to the debtor is required. Imagine that a company wishes to assign to a factor payments due to it from customers. While the same assignation can be used to assign multiple claims, the individual assignations cannot be completed unless there is intimation of the assignation to each customer. There are thus three stages to the transfer: (a) the contract to assign; (b) the execution and delivery of the assignation document; and (c) the intimation to the debtor. Without intimation there is no transfer. Intimation can be described in property law terms as an "external act", because it publicises the transaction beyond the parties.[1]

5.2 For the assignation of multiple claims, the current law is costly and cumbersome. Undoubtedly reform is needed. The question is how best to effect that. In many other legal systems such as Germany and South Africa, and under international instruments such as the DCFR no external act is required to complete an assignation.[2] This is the position too in English law for equitable assignment,[3] as well as now being the law in France following amendments to the French Civil Code in 2016.[4] In the Discussion Paper, we set out a number of arguments against abolishing the need for intimation and not requiring any external act.[5] In the first place, the assignee is generally going to have to intimate anyway so as to obtain payment from the debtor. But this is not a conclusive argument. In many commercial arrangements, for example securitisations and invoice discounting, the parties wish the assignor to continue to collect the receivables which are assigned but remit the proceeds to the assignee.

5.3 In the second place, dispensing with an external act runs contrary to the publicity principle of Scottish property law, but it is not clear that this argument is as strong for claims as, say, for land. The existence of a piece of land is self-evident, land is permanent and it is in the public interest that its ownership is registered. Claims, however, have no physical existence, are ephemeral and arise without publicity. Moreover, intimation is a very weak form of publicity.[6]

5.4 Thirdly, requiring an external act makes fraud more difficult. The time of the intimation is the time that the debtor is told. Without participation in the fraud by the debtor, the time cannot be falsified. Economic efficiency is also promoted, because third parties can

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[1] But compared with registration the level of publicity is very limited.
[2] See Discussion Paper, Appendix B. See also A F Salomons, "Deformalisation of Assignment Law and the Position of the Debtor in European Property Law" (2007) 5 European Review of Private Law 639 and C Lebon, "Property Rights in Respect of Claims" in S van Erp and B Akkermans (eds), *Cases, Materials and Text on Property Law* (2012) 365 at 387–403.
[3] See eg G Tolhurst, *The Assignment of Contractual Rights* (2nd edn, 2016) ch 4.
[4] See French Civil Code art 1323 (in force 1 October 2016).
[5] Discussion Paper, paras 14.5–14.12.
[6] See R G Anderson and J W A Biemans, "Reform of Assignation in Security: Lessons from the Netherlands" (2012) 16 EdinLR 24 at 34.

check the position by reference to the external act.[7] Thus a would-be purchaser of a claim can inquire with the debtor as to whether any preceding assignation has been intimated to him or her.

5.5 We noted also in formulating our policy that a link requires to be made between assignation of claims and security over claims. This is the approach in the USA, because in practice an outright assignation and an assignation in security can appear indistinguishable. UCC–9 and the PPSAs require registration for the outright assignment of certain types of claim, such as receivables, but not for all types of claim, for *priority* purposes.[8] Under these systems a distinction is drawn between "attachment" (effectiveness between the parties, here the assignor and assignee) and "perfection" (priority in a question with third parties, for example, another assignee of the same claim). Scottish property law does not recognise the attachment/perfection distinction.[9] One of its general principles is that the creation, transfer, variation or extinction of a property right is good against the world or it is good against nobody. We noted also that requiring registration in some cases but not others introduces an element of complexity, which may be undesirable.

5.6 We canvassed the possibility of the way forward in Scotland being to give assignees the option of intimation or registration. The approach would be more flexible than UCC–9 and the PPSAs. The law would thus accommodate both large-scale transactions as well as small one-off transactions. In the former, registration would typically be used. Where the registration option was taken, good faith debtors would be protected. Debtors could not be expected to check the register as to do so would involve time and expense and there is a fundamental principle, which we discuss later,[10] that the debtor is not to be prejudiced by the assignation. We mentioned also an alternative possibility of requiring registration in all cases, but considered that to be unwise, not least because it is not the approach of UCC–9 and the PPSAs.

Consultation

5.7 After setting out the various options, the Discussion Paper put four to consultees:

(1) Keep the current law, which requires intimation, albeit with certain revisions.

(2) Abandon the need for intimation. Transfer should happen solely by the mutual consent of the cedent and the assignee. (But with protections for the account debtor who acts in good faith.)

(3) Adopt something like the UCC approach: abolish the requirement of intimation, and introduce registration for some cases; for other cases transfer would

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[7] But cf A McAlpine, "Raising finance over claims to payment and reform to the law of outright assignation" 2015 Juridical Review 275 at 314.

[8] The UNCITRAL Convention on the Assignment of Receivables in International Trade in its optional annex also contemplates a system of priority by registration. See N O Akseli, "The United Nations Convention on the Assignment of Receivables in International Trade and Small Businesses" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 465 at 475–479.

[9] In the Discussion Paper, we consulted on the introduction of such a distinction as regards security rights. Consultees did not support this. See volume 2 of this Report.

[10] See paras 12.27–12.34 below.

happen solely by the mutual consent of the cedent and the assignee. (But with protections for the account debtor who acts in good faith.)

(4) Maintain the requirement of an external act in all cases, but give the parties the choice of registration or intimation.

We said that we provisionally inclined towards the fourth option.

5.8 Consultees were split on this question. Perhaps unsurprisingly, no-one favoured option (1), keeping the current law. Only David Cabrelli supported option (3). A slim majority of those who responded to the question favoured option (4). These included ABFA, the Law Society of Scotland, the WS Society and several law firms. In contrast, Chris Dun, John MacLeod and Scott Wortley favoured option (2). Dr Ross Anderson originally supported an approach which would replace intimation with a requirement for notarial execution or registration in the Books of Council and Session,[11] but subsequently favoured option (2).[12]

Policy

5.9 We have found this policy matter a difficult one and we have discussed it in some detail with our advisory group. Ultimately we hold to the view to which we inclined in the Discussion Paper and which had most support from consultees. We believe that an assignation should either be completed by intimation to the debtor,[13] or by the assignee registering the assignation in the new Register of Assignations.[14] Our reasoning is developed from some of the above discussion. First, the approach offers flexibility.[15] Undoubtedly factors and invoice discounters would prefer the registration option but one-off transactions could continue to be completed by intimation. The approach also provides continuity with the existing law in still requiring an external act, either intimation or registration. This prevents fraudulent ante-dating.

5.10 Our view is that since registration would be the normal method of assigning multiple receivables and future receivables[16] this would promote economic efficiency because it would allow other parties dealing with the assignor to know whether the claims have already been assigned for financing purposes. Registration, which would be online,[17] should be easy and inexpensive, and therefore we think it is attractive because of the benefits it would offer.

5.11 We are also influenced by the fact that the intimation/registration approach was favoured by ABFA (now part of UK Finance) which represents the factoring and invoice discounting industries in the UK and Ireland. We think that its view commands particular weight here.

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[11] See R G Anderson, "A Critique" (2012) 16 EdinLR 267. See also R G Anderson and J Biemans, "Reform of Assignation in Security: Lessons from the Netherlands" (2012) 16 EdinLR 24.
[12] Dr Anderson was a member of our advisory group.
[13] On intimation, see paras 5.23–5.63 below.
[14] See Chapters 6 to 11 below.
[15] But for an important counter argument see para 5.19 below.
[16] See paras 5.81–5.97 below. In particular because intimation is impossible in the case of a future claim where the debtor is unknown.
[17] See paras 6.33–6.39 below.

5.12 Moreover, a "no-registration-at-all" approach is unusual when comparative models are considered. UCC–9, the PPSAs, the DCFR and the UNCITRAL Model Law on Secured Transactions require assignations in security by anyone to be registered for the purposes of priority.[18] Indeed, under UCC–9, the PPSAs and the UNCITRAL Model Law registration of the outright assignation of certain types of claim, typically receivables, is also required for these purposes.

5.13 One of the main counter-arguments against registration is that it means a lack of confidentiality.[19] But, in its response on this issue, ABFA viewed the desire for confidentiality as not being strong.[20] Many of the other current ways in which a business obtains funds have to be registered (eg the granting of a floating charge or standard security). And any assignation in security granted by a company has to be registered in the Companies Register under the current law.[21]

5.14 Another concern, highlighted in particular by Scott Wortley, is that because registration is not a requirement for equitable assignments in England, parties would continue to write contracts under English law. But we understand from another member of our advisory group, Bruce Wood, that having to write contracts involving only Scottish parties under English law results in increased costs and that the factoring and invoice discounting industries would prefer the new registration option. Moreover, there is uncertainty as to the efficacy of using English law following the decision in *Joint Administrators of Rangers Football Club Plc, Noters.*[22]

5.15 There is also pressure to reform English law here because the current law is regarded as unsatisfactory. In a Discussion Paper on Secured Transactions Reform published in 2012 the City of London Law Society's Financial Law Committee recommended that consideration should be given to establishing a register of outright transfers of receivables. Its purpose would be to regulate the priority of such transfers against third parties.[23] In other words, the assignment would be effective as between assignor and assignee by mere agreement, but registration would be needed to make it effective against third parties. The draft Secured Transactions Code subsequently issued by the Committee makes provision for the registration of assignments of receivables for priority purposes.[24]

5.16 In 2014 the Secured Transactions Law Reform Project held a seminar to explore and discuss the merits of an online register for all security interests, including outright assignments of receivables.[25] In a Discussion Paper issued in 2017 the group proposed

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[18] In the UK this of course is currently required only for companies etc.
[19] This point is made forcefully in A McAlpine, "Raising finance over claims to payment and reform to the law of outright assignation" 2015 Juridical Review 275 especially at 313–315.
[20] Although elsewhere ABFA stated that there were confidentiality issues with supplying a copy of the assignation as part of intimation. See para 5.46 below. Elsewhere we recommend a power to allow certain information within the assignation document to be redacted. See para 11.46 below.
[21] Companies Act 2006 Part 25. See Chapter 36 below.
[22] [2012] CSOH 55. See para 3.16 above and paras 15.30-15.32 below.
[23] See http://www.citysolicitors.org.uk/attachments/article/121/20121120-Secured-Transactions-Reform---discussion-paper.pdf.
[24] City of London Law Society draft Secured Transactions Code ss 35 and 38.
[25] See http://securedtransactionslawreformproject.org/past-events/.

reform along broadly the same lines as the Committee's draft Code.[26] Registration of an assignment of receivables would be required for priority purposes. We note also that the Security Interests (Jersey) Law 2012 introduced registration of assignments of receivables and that the assignment registered first normally has priority.[27]

5.17 Scottish law could be reformed along similar lines, so that registration is only needed for third party effectiveness. In response to our draft Bill consultation of July 2017 Professor Hugh Beale and Professor Louise Gullifer, two leading experts in English law, strongly advocated this approach and criticised requiring registration for "constitutive" as opposed to priority purposes. They pointed out that assignations, unlike security rights, will generally not engage insolvency law and that requiring registration to effect transfer between assignor and assignee is undesirable. But adopting a "priority" approach would be to introduce "limping"[28] rights, that is to say a right enforceable against some parties and not others. As we have noted already, this approach is contrary to the general principles of our property law. Here is Professor Kenneth Reid, writing on the current law: "What an unintimated assignation cannot do is to transfer the property in a question between [assignor] and assignee but not in a question between the assignee and third parties. That is an impossibility in our law of property. Ownership is either with one party or it is with another party. It cannot be with one party for some purposes and with another party for other purposes. There is no such thing as a personal right of ownership: ownership is necessarily a real right."[29] And in the words of Lord Hodge: "There is no such thing as a 'quasi real right'".[30]

5.18 We think that adopting an approach which runs counter to the underlying principles of our law would be problematic. It is worth observing that this also rules out the following possibility: (a) assignation effective without intimation or (b) assignation effective by registration. If an assignation is effective against the world by mere contract there can logically be no purpose in registering.

5.19 We are aware also that in its 2017 Discussion Paper, the Secured Transactions Law Reform Project criticises the "combined system" of intimation/registration on the basis that a third party cannot solely rely on the register. They have to make enquiries with the account debtor too, which "defeat[s] the purpose of the register".[31] This point has also been made to us directly by Professor Beale and Professor Gullifer. It is perhaps the main counter-argument to the proposition stated above that the intimation/registration approach offers flexibility. While this argument has some force, we think that it overstates the problem. Under our scheme we expect that assignations of receivables in favour of financiers would invariably be registered because this would be much simpler and cheaper than intimations to multiple debtors. Moreover, intimation would not be an option for future claims. We

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[26] Secured Transactions Law Reform Project, Discussion Paper Series: Sale of Receivables (2017) available at https://securedtransactionslawreformproject.org/2017/01/03/january-2017-discussion-papers/. The author is Professor Hugh Beale.
[27] Security Interests (Jersey) Law 2012 art 29(1)(a).
[28] See G L Gretton, "Security over moveables in Scots law" in De Lacy (ed), *The Reform of UK Personal Property Security Law* 270 at 278. In this regard Scottish property law is like German property law and contrasts with English law as well as property law in France and jurisdictions based on French law. Cf French Civil Code arts 1323 and 1324.
[29] K G C Reid, "Unintimated Assignations" 1989 SLT (News) 267 at 269.
[30] *3052775 Nova Scotia Ltd v Henderson* [2006] CSOH 147 at para 11. There are a few exceptions to this. For example, occupancy rights under the Matrimonial Homes (Family Protection) (Scotland) Act 1981 and the Civil Partnership Act 2004 are enforceable against some parties, but not others.
[31] Secured Transactions Law Reform Project, Discussion Paper Series: Sale of Receivables para 3.D.iii.

anticipate that the register would be definitive in such cases. Moreover, a prospective assignee is effectively only at risk from a fraudulent or negligent assignor who does not disclose that the claim has already been assigned by intimation. Our advisory group were of the view that financial institutions factor in such risks. Indeed under the current law there is the risk that the same claim is assigned more than once and an intimation of a rival assignation reaches the debtor first.

5.20 The Secured Transactions Law Reform Project's proposals (and indeed those of the City of London Law Society) are aimed only at receivables. Broadly speaking, this means invoices under contracts for goods, services or incorporeal assets, in other words the types of claim which are usually the subject of factoring and invoice discounting. Other claims are excluded. On the other hand, our recommendations relate to claims in general. We think therefore that there would be merit in giving Scottish Ministers the power to specify types of claim for which registration would be compulsory to transfer the claim. In such cases, intimation would be ineffective.[32] Thus if registration for assignation of receivables effectively became compulsory in England and Wales, albeit there only to achieve priority against third parties, there might be support for this in Scotland too.

5.21 Finally, it should be mentioned that the claim would not necessarily transfer at the time of intimation or registration. It might not yet be identifiable as a claim to which the assignation document relates, it might not yet be held by the assignor or the assignation might be subject to a condition which requires to be satisfied for there to be transfer.[33]

5.22 We recommend:

9. A claim should be transferred on:

(a) the assignation being intimated to the debtor, or

(b) the assignation being registered in the Register of Assignations,

but the Scottish Ministers should have the power to specify categories of claim where registration is required for transfer.

(Draft Bill, s 3(1), (2)(b) & (6))

Intimation: terminology

5.23 We have recommended that it should continue to be possible to complete an assignation by intimation to the debtor (as well as there being the alternative of registration in the RoA). A further question is whether the term "intimation" should continue to be used. In English law and in international instruments the relevant term is "notification".[34] The debtor is "notified" of the assignment. We asked consultees whether "intimate/intimation" should be replaced by "notify/notification". A range of views was expressed here. For

[32] In relation to transfer, but we think that the debtor should be discharged where they perform in good faith to an assignee who intimates but does not register. See paras 12.12–12.15 below.
[33] See paras 4.25–4.30 above and paras 5-73–5.97 above.
[34] See, for example, Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* paras 7.90–7.99; DCFR III.–5:119 and 120.

example, ABFA and the WS Society supported replacement. The Aberdeen Law School disagreed, referring to the fact that "intimations" are read out in churches to convey information to congregations. The Judges of the Court of Session did not think that "the present language creates any real problems." The Law Society of Scotland saw "no compelling reason for such a change." The Faculty of Advocates said that the term "intimation" is established legal terminology, well understood and used without difficulty." Others did not have a strong view.

5.24 In the absence of strong support for change, we recommend:

10. "Intimate/intimation" should not be replaced by "notify/notification".

5.25 As will be seen, however, we recommend below that serving a notice of the assignation on the debtor is a method (indeed the usual method) by which intimation is effected.[35]

Intimation: rationale

5.26 Dr Ross Anderson has identified three rationales for the requirement of intimation to the debtor.[36] The first is to provide *publicity*. But, as we have noted already,[37] this rationale is weak because the level of publicity is low. Only the debtor requires to be told and not the world via a register. The second is *debtor protection*. Until the debtor is informed of the assignation, performance can continue to be made to the assignor. The third is certainty on insolvency and competition, or to put it another way, *priority*. The requirement for intimation enables a court to decide who the creditor in a claim is, when that creditor became the creditor, and to how much that creditor is entitled. In the case of two or more fraudulent assignations of the same debt, intimation determines priority. The first assignee to intimate prevails.[38]

5.27 There has been some tendency in Scotland to conflate the rationales.[39] We think, however, that the better approach is to separate the issues of priority and debtor protection. In the words of Dr Hamish Patrick in his response to the Discussion Paper: "A possible distinction may be drawn between notice as a means of completing title (ie as an external provable priority point) and notice as a means of protecting an account party who pays the assignor. The knowledge and understanding of the account party is irrelevant to the former." For example, the assignee may duly post the intimation by recorded delivery to the debtor, but it may be signed for by someone living with the debtor who does not hand it over. Certainly, the debtor should be protected if performance is made to the assignor, but it would also seem fair that the assignee should prevail against the assignor's creditors in the event of the assignor's insolvency, if the assignee can prove that the intimation was posted.

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[35] See paras 5.38–5.57 below.
[36] Anderson, *Assignation* paras 6-04 to 6-13. See too B Stephen, "Scotland" in W Johnston (ed), *Security Over Receivables: An International Handbook* (2008) para 30.10 and, in an Australian context, G Tolhurst, *The Assignment of Contractual Rights* (2nd edn, 2016) 77–78.
[37] See para 5.3 above.
[38] But arguably subject to the rule on "offside goals". See Anderson, *Assignation* paras 11-04–11-31.
[39] As noted by R G Anderson, "Intimation 1862-2008" (2008) 12 EdinLR 275. See also G Lubbe, "Assignment" in H MacQueen and R Zimmermann (eds), *European Contract Law: Scots and South African Perspectives* (2006) 307 at 313–318 and R G Anderson and J W A Biemans, "Reform of Assignation in Security: Lessons from the Netherlands" (2012) 16 Edin LR 24 at 29.

Another example is where the intimation physically reaches the debtor but the debtor does not bother to open the envelope. A third is where the intimation is in small print in the midst of a long document which the debtor does not understand.

5.28 We consider therefore that the law would be improved by having (a) rules on what is necessary for intimation to achieve priority and (b) separate rules on debtor protection. Under the recommendation which we made above,[40] it would also be possible to achieve priority by registration, but the rules on debtor protection would apply in that situation too.

Intimation: current law

5.29 As we saw above, at common law it was necessary for intimation to be carried out notarially, although there were certain exceptions.[41] The Transmission of Moveable Property (Scotland) Act 1862 introduced a less onerous form of notarial intimation as well as a non-notarial method.[42] The latter involves sending a certified copy of the assignation to the debtor by post.

5.30 We understand that the common law notarial method is unknown in practice today, although it remains competent. The less onerous notarial method introduced by the 1862 Act is, we understand, occasionally used, in cases where evidence of intimation is wanted but it is thought that the debtor is unlikely to give a written acknowledgement. In its response to the Discussion Paper, the WS Society commented: "Notarial intimation is a dead letter and only resorted to in a few serious situations."

5.31 The 1862 Act postal method is used, but not always. Often, notice is sent by post, but without a copy of the assignation.[43] In *Christie Owen & Davies plc v Campbell*[44] the court said that to intimate is to inform. If this is correct then none of the three methods just mentioned[45] is necessary. Bruce Wood has written that following this "judicial comment (though perhaps obiter) at Appellate Court level, it seems reasonably clear that intimation can be made without having to give the debtor a copy of the assignation and the debtor's acknowledgement is not required."[46] But since there was no competing third party in the case the effectiveness of the intimation was not tested.[47] It is unsatisfactory that the law should be uncertain, whatever view is taken as to what the law should be.

5.32 While intimation is traditionally made by the assignee, there is also authority for intimation by the assignor being permissible.[48] This is sometimes done in practice and has

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[40] See paras 5.1–5.22 above.
[41] See para 3.9 above.
[42] 1862 Act s 2.
[43] Often the notice is in small print, and often the account party is not asked to make any arrangements to pay the transferee, because the assignor and assignee arrange for the latter to take control of the account into which the account party is paying.
[44] [2009] CSIH 26, 2009 SC 436. *Libertas-Kommerz GmbH v Johnson* 1977 SC 191 is often cited as supporting a low threshold for intimation. But much proceeded on concessions by counsel. See footnotes 30, 38 and 39 in ch 7 of Anderson, *Assignation*.
[45] See para 5.29 above.
[46] R B Wood in Ruddy, Mills and Davidson, *Salinger on Factoring* para 7.57. And see also *Promontoria (Ram) Ltd v Moore* [2017] CSOH 88.
[47] R G Anderson, "A Strange Notice" (2009) 13 EdinLR 194.
[48] Anderson, *Assignation* para 6-30.

the advantage that the assignor is the party with whom the debtor has the existing relationship.

5.33 There are also two equivalents[49] to intimation clearly recognised by the common law. The first is actings of the debtor acknowledging the assignation. For example, if the debtor, having heard informally of the assignation, performs to the assignee then this dispenses with the need for intimation.[50] The second is founding on the assignation in judicial proceedings.[51] For example, the assignee raises an action against the debtor for performance. In *Carter v McIntosh*[52] the production of an assignation in a multiplepoinding was described by Lord Justice-Clerk Inglis as "the best of all intimations, because it was a judicial intimation."[53]

Reform of intimation: general

5.34 The uncertainty in the current law is unsatisfactory and detrimental to the needs of business. We consider that there should be clear modern statutory rules. In discussions with our advisory group we have concluded that there should only be three ways in which an assignation can be intimated. First, this may be done by written notice to the debtor. This would be the usual method and would include electronic notice. The second would be the debtor acknowledging to the assignee that the claim is assigned. This might be by performance by the debtor to the assignee, or a promise to perform to the assignee by the debtor of something which the assigned claim obliges the debtor to perform. The third would be by the debtor being party to judicial proceedings in which the assignation is founded on. We describe these in more detail in the following sections.

5.35 We reflected on whether to retain notarial intimation, given that currently it is recognised at common law and under the 1862 Act. But our advisory group advised that its rarity of use did not justify that. Moreover, there would be nothing to stop our recommended method of intimation by written notice being effected by a notary, although no special status would be given to such an intimation.

5.36 The effect of our reforms would also be that the 1862 Act would no longer be needed and could be repealed.

5.37 We therefore recommend:

11. Intimation of the assignation of a claim should be effected and only effected:

(a) by there being served on the debtor written notice of the assignation,

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[49] Or "equipollents". See Anderson, *Assignation* para 7-11.
[50] See McBryde, *Contract* para 12-96 citing *Inverlochy Castle Ltd v Lochaber Power Co* 1987 SLT 466.
[51] For title to sue all that is required is that the pursuer has a contract to receive an assignation. The assignation can be subsequently produced during the proceedings. See *Morris v Rae* [2012] UKSC 52, 2013 SC (UKSC) 106 at paras 52 to 55.
[52] (1862) 24 D 925.
[53] At 934. But compare Anderson, *Assignation* paras 7-16 to 7-23. See also *Promontoria (Ram) Ltd v Moore* [2017] CSOH 88 at paras 43 and 94 per Lord Bannatyne.

(b) by the debtor acknowledging to the assignee that a claim is assigned, or

(c) by it being intimated to the debtor, in judicial proceedings to which the debtor is a party, that the assignation is founded on in the proceedings.

12. The Transmission of Moveable Property (Scotland) Act 1862 should be repealed.

(Draft Bill, ss 9(1) and 41)

Intimation by written notice to the debtor

By whom?

5.38 As under the current law, written notice would be the usual form of intimation. We have considered whether this should be capable of being given only by or on behalf of the assignee, or also by or on behalf of the assignor. Under general property law principles it is the transferee who completes the steps necessary to transfer property. Thus in the transfer of land the disposition is always registered by or on behalf of the transferee in the Land Register and not by or on behalf of the transferor. This suggests therefore that only assignees should be able to intimate and thus "press the button" to acquire the claim.

5.39 But for assignation there is a strong counter-argument. It is the assignor whom the debtor knows. It is the assignor with whom there is an existing contractual relationship. The assignee on the other hand may well be a stranger. The debtor may well accept the fact of the assignation more easily if he or she is informed of it by the assignor. Intimation by the assignor appears competent at common law[54] and our advisory group strongly supported it being available under the new statutory regime. They commented that the arrangements for intimation would normally be governed by contractual provisions entered into by the assignor and an assignee. Therefore an assignor who "jumped the gun" and intimated prematurely would be liable for breach of contract. Intimation should of course also be competent by means of an agent, such as a solicitor.

5.40 We recommend:

13. Where intimation is by means of written notice to the debtor, it should be possible for the notice to be served by or on behalf of either the assignor or assignee.

(Draft Bill, ss 9(1)(a) and 118(4))

Content of notice

5.41 We asked consultees whether notification, to be effectual, should be in such a form as to bring home its meaning to a reasonable account party. Consultees generally agreed.

[54] See para 3.10 above.

While, as set out above,[55] we have refined our thinking to draw a distinction between intimation for the purpose of priority and intimation for the purpose of debtor protection, we consider that there should be certain pre-requisites for the notice, without which it should fail.

5.42 As under the current law, the notice should be in writing. We think it self-evident that it should include the name and address of the assignor and the assignee, and provide details of the claim (or part of claim) being assigned. The debtor requires this information. Where the notice is sent electronically[56] we think that it should be possible for it to supply an electronic link to a website or portal where the details of the assignation are set out.[57]

5.43 We consider that the notice could be signed by the assignee, assignor or a third party such as an agent, but do not think that this is essential. We understand that factoring of invoices is commonly done by a sticker being added to the invoice informing the debtor of the assignation and that payment should be made to the assignee. The stickers are not signed. We are doubtful of any benefit that would be gained by insisting on such stickers being signed, particularly given the recommendations which we make below, in relation to debtors having rights to information and being protected where the wording of a notice is unclear.[58]

5.44 Where factoring is carried out by means of stickering, the details of the claim will be on the invoice and the details of the assignation on the sticker. We see nothing objectionable in this.[59] It should be possible for the notice to consist of, or be contained within, a single document or more than one document. "Document", in this context, should include an e-mail or an attachment to an e-mail.

5.45 There was support from several consultees for a form of model notice. This would not be compulsory but, if used, the parties would have the comfort of the wording being approved by statute and therefore not open to argument about being insufficiently clear. We agree and the draft Bill provides the Scottish Ministers with the power to prescribe a model notice. This notice is for assignation of monetary claims, which is the paradigm case. But it would be possible to adapt it for an assignation of a non-monetary claim.

5.46 As we have seen, under the postal method in the 1862 Act it is necessary to send the debtor a copy of the assignation. This requirement was roundly criticised by ABFA in its response. It commented that it was "completely impractical" in bulk transfers to give copies of the assignation document to individual debtors as the document may be very lengthy and full of confidential information.[60] The WS Society made similar points. We accept the force of these submissions and agree that a copy of the assignation should not require to be

[55] See paras 5.26–5.28 above.
[56] See para 5.51 below.
[57] We were advised by Burness Paull LLP that portals are often used in certain commercial transactions to provide information to relevant parties.
[58] See Chapter 12 below.
[59] We expect that factors would register assignations in the Register of Assignations too, but there may be circumstances in which they do not or that due to a mistake the registration is ineffective. Therefore ensuring that intimation by stickering results in transfer of the claim remains important.
[60] As to how the desire for confidentiality would operate in relation to registration, see paras 6.21 and 6.28 below.

served with the notice. Instead the assignee should have certain information duties to the debtor, which we set out below.[61]

5.47 We therefore make the following recommendations in relation to content of the notice:

14. A notice of an assignation:

(a) should

(i) set out the name and address both of the assignor and assignee, and

(ii) provide details of the claim assigned (or, in the case of a claim assigned in part, both of the claim and of the part assigned),

but where the notice is transmitted electronically it can provide an electronic link to a website or portal containing this information,

(b) should not require to be executed or authenticated,

(c) if the claim is a monetary claim, may but need not be in a form prescribed by the Scottish Ministers, and

(d) may consist of, or be contained within:

(i) a single document, or

(ii) more than one document,

and "document" should be defined to include an e-mail or an attachment to an e-mail.

(Draft Bill, s 9(3) & (5))

Service of notice

5.48 The notice requires to be given to the debtor. The formal legal word is "served". Section 26 of the Interpretation and Legislative Reform (Scotland) Act 2010 makes general provision for where a document requires to be served under an Act of the Scottish Parliament. We think that it makes sense to adopt its provisions, but with some amendments.

5.49 There are three methods by which service may be effected under section 26. First, the document can be delivered personally to the debtor. We consider that this rule should apply without amendment.

[61] See paras 12.17–12.26 below.

5.50 Secondly, section 26 enables the document to be sent by a registered or recorded postal service to the "proper address" of the debtor. The "proper address" for bodies corporate is the address of the registered or principal office of the body, for partnerships is the address of their principal office[62] and, in any other case, is the last known address of the debtor. We consider that for the purposes of intimation ordinary post should be permissible rather than recorded delivery being mandatory. We are advised that factors currently use ordinary post and we do not consider that insisting on registered or recorded post is necessary. That said, using ordinary post is more difficult to prove, but that is a risk for assignees to weigh up. Alternatively, we think that it should be possible for a private courier to be used.[63] In current factoring practice intimation will be made to the address of the debtor which appears on the relevant invoice, in other words the address which the debtor has provided to the assignor when contracting with the assignor. We consider that intimation to that address should also be permissible.

5.51 Thirdly, section 26 allows the document to be sent electronically if the person authorised or required to serve the document and the person on whom it is to be served agree in writing (a) that electronic service is possible; (b) as to the form of electronic service; and (c) the address to which the service is made. We consider that a relaxation of this is appropriate for present purposes and that the notice may be transmitted electronically where the debtor has provided the assignor with an e-mail address for electronic communication purposes. Nowadays this will often be the typical route of communication.

5.52 Section 26 also has provisions deeming when service has taken place. In the case of postal service on an address in the United Kingdom,[64] or in the case of electronic delivery, this is 48 hours after the document was sent, unless the contrary is shown. Our present subject is that of priority of assignations (we deal with debtor protection separately in Chapter 12 below). Certainty is an important aspect of that. We therefore consider there should be a more objective rule that postal or electronic service is taken to be effected 48 hours after the notice was sent, unless it can be shown to have been received earlier.

5.53 For example, Laura owes Kirk £1,000. On Monday, Kirk fraudulently assigns the claim twice, first to Max and then to Neil. On Tuesday, Max posts a notice of intimation to Laura. On Wednesday, Neil posts a notice of intimation to Laura. Max's notice will be taken to be served on Thursday and Neil's on Friday. Therefore Max will be successful, unless Neil can prove that Laura received his notice first. The difficulty with the "unless the contrary is shown" formula in section 26, is that it might be proven that neither of the notices actually reached Laura. In these circumstances, we consider that Max should still have effected a valid assignation provided he can prove that he sent the notice (but Laura would be protected by the debtor protection rules discussed below in Chapter 12).

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[62] In its response to our draft Bill consultation of July 2017 ICAS argued that "any established place of business of the partnership" would be preferable. In its response R3 suggested that "principal office" should be defined. We are, however, reluctant to deviate much from the wording used in section 26 of the 2010 Act. Further, our recommendation made below that effective intimation can be made to an address (postal or electronic) provided to the assignor by the debtor should assist here.

[63] Although we note that in *Hoe International Ltd v Andersen* [2017] CSIH 9, the Inner House interpreted a contractual provision to the effect that delivery by means of the DX system used by solicitors qualifies as "personal delivery". Compare *Ener-G plc v Hormell* [2013] 1 All ER (Comm) 1162.

[64] The legislation is silent on addresses outside the United Kingdom, where evidence of the addressee actually receiving the notice is presumably required.

5.54 For electronic intimation, notwithstanding the fact that section 26 provides for a period of 48 hours as to when service is deemed to take place, following discussions with our advisory group and others,[65] we consider that a 24 hour period is more appropriate given the faster speed of electronic communications. Once again it will always be open to the assignee to prove that delivery was effected more quickly. A delivery receipt for an e-mail would be useful evidence in this regard.

5.55 We believe also that it should be open to the debtor and holder of a claim (or a party whose unilateral undertaking (promise) gives rise to the claim) to have some autonomy with regard to the notice provisions. They should be able to specify that only one (or more) of the methods of service is competent. Thus they might decide that the intimation notice may only be sent electronically. They should also be able to specify a particular address to which an intimation notice must be sent, rather than the "proper address"[66] or an address that has been previously provided by the debtor to the assignor.

5.56 Finally, we think that it should be possible for intimation to be made or received by duly authorised representatives of the parties, such as their solicitors.

5.57 We therefore recommend:

15. (a) A notice of an assignation should require to be served:

(i) by being delivered personally to the debtor,

(ii) by being sent by post or by courier either to the proper address of the debtor or to an address for postal communication provided to the assignor by the debtor,

(iii) by being transmitted to an electronic address provided to the assignor by the debtor.

(b) The proper address of the debtor should be:

(i) in the case of a body corporate, the address of the registered or principal office of the body,

(ii) in the case of a partnership, the address of the principal office of the partnership, and

(iii) in any other case, the last known address of the debtor.

(c) Where a notice is posted to an address in the United Kingdom, it should be taken to have been received 48 hours after it is sent unless it is shown to have been received earlier.

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[65] Notably Professor Andrew Murray of the London School of Economics, an expert in information technology law.

[66] See para 5.50 above.

(d) Where a notice is sent electronically, it should be taken to have been received 24 hours after it is sent unless it is shown to have been received earlier.

(e) The debtor and the holder of the claim (or the person whose unilateral undertaking gives rise to the claim) should be able in writing to determine that:

(i) only certain of the above methods of service are to apply as respects the claim, or

(ii) postal service is to be to a specified address of the debtor.

(f) It should be competent for intimation to be made or received by authorised representatives of the parties.

(Draft Bill, ss 9(4) & (6) to (13) and 118(4))

Notice by assignee instructing the debtor to perform to the assignor

5.58 The parties to the assignation may wish, notwithstanding the assignation for the debtor to continue to perform to the assignor. For example, it might be convenient in an invoice finance transaction for the customers of the assignor to make payment to that party rather than to the finance company. The assignor would then arrange for the money to be transferred. Protections such as trusts would be put into place to protect the assignee in the event of the assignor's insolvency. Another situation is project funding where income streams are assigned in security to a bank. But the bank only needs to collect the income if the debtor company defaults. In the meantime the streams should continue to be collected by the company.

5.59 There is currently some doubt in Scottish law as to whether it is permissible for an intimation to instruct the debtor to perform nevertheless to the assignor.[67] We consider that in the interests of commercial certainty the position should be clarified. There seems no compelling reason why the notice, while alerting the debtor to the fact of the assignation, should not be able to state that performance must still be made to the assignor. In the case of money being payable, the assignor may be viewed as the assignee's agent in relation to the collection of that money.

5.60 The inter-relationship between such an arrangement and the law of diligence is one of some nicety. What happens if a creditor of the assignee seeks to arrest in the hands of the debtor, who has been instructed to pay to the assignor? There is an arguable difference between an outright assignation and an assignation in security here, on the basis that in the latter the assigned claim is protected from the assignee's personal creditors.[68] But it is impossible to state the position with certainty. A debtor faced with an arrestment in such a situation would therefore be best advised to seek a multiplepoinding.

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[67] In the Discussion Paper, para 11.14 fn 28 we highlighted Hume, *Lectures* III, 5 and *Hope and McCaa v Wauch* 12 June 1816, FC. For criticism of *Hope* see R G Anderson and J W A Biemans, "Reform of Assignation in Security: Lessons from the Netherlands" (2012) 16 Edin LR 24 at 29–30.

[68] *Purnell v Shannon* (1894) 22 R 74.

5.61 We recommend:

16. Any rule of law whereby an assignation is rendered ineffective by an instruction by the assignee to the debtor to perform to the assignor should be abolished.

(Draft Bill, s 17(1)(b))

Intimation by the debtor acknowledging to the assignee that the claim is assigned

5.62 Intimation should also be effected by the actings of the debtor towards the assignee, acknowledging the assignation. The debtor, having heard informally of the assignation, might promise to the assignee that performance will be made to the assignee, or performance might actually be made to the assignee.[69]

Judicial intimation

5.63 The final form of intimation should be where the debtor is party to judicial proceedings in which the assignation is founded on. Thus the assignee may sue the debtor for payment of the debt due under the claim which has been assigned. Of course, under the current law it would be normal to expect a notice of assignation to have been sent first and intimation to have already taken place by virtue of that.[70] Even under our recommendations, whereby assignations may be effected by registration in the RoA, we would still anticipate that intimation (to require the debtor to pay to the assignee) would usually take place by notice rather than court action. Nevertheless, we consider that this form of intimation should remain competent as an option. Something may have gone wrong with the notice of assignation (for example, it might never have been sent) which does not transpire until later on. Judicial intimation gives the assignee an alternative means of establishing the priority of the assignation.[71]

5.64 The time at which intimation would take place would be when intimation is made to the debtor in judicial proceedings that the assignation is founded on in those proceedings. It must be remembered that the rule here only concerns completion of the assignation. The question as to whether the debtor should be protected if they still perform to the assignor is a separate one.[72] It would depend on whether the debtor can be regarded as being in good faith.[73]

Co-debtors

5.65 A claim may be enforceable against more than one person. For example, Jules and Jim might borrow £10,000 from Kevin. Kevin would then have a claim against them both for repayment of the £10,000. He might assign that to Lena. The current law as to intimation to co-debtors is expressed succinctly by Professor Reid: "in the case of joint debtors, intimation

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[69] See para 5.33 above.
[70] Anderson, *Assignation* para 7-23.
[71] Where the parties have entered into arbitration rather than judicial proceedings, it would of course be possible for intimation to take place by notice under the recommendations made in para 5.45 above.
[72] See Hume, *Lectures* III, 9 doubting whether mere citation not followed by judicial production of the assignation amounts to judicial intimation. See also Anderson, *Assignation* para 7-17.
[73] See paras 12.1–12.8 below.

to one completes the transfer, but intimation to all is necessary to prevent payment to the cedent".[74] In other words, in our example, if intimation is made by Lena to Jules alone, this will transfer the claim. But if Jim, in ignorance of the assignation, pays Kevin the £10,000 rather than Lena, the debt will be discharged and payment will not require to be made to Lena.[75] We think that this policy is correct and should continue to be the law.

5.66 We therefore recommend:

17. Where there are co-debtors, intimation to any one or more of them should be treated as intimation to all of them.

(Draft Bill, s 9(2))

Priority

5.67 The current law is that priority/ranking of assignations is tied to completion of title. Thus in the case of competing assignations the one which is intimated first wins. In a competition between an assignation and an arrestment, the priority point for the former is the time of intimation.[76]

5.68 In legal systems which do not require intimation the priority point is often the act of assignment (the parties' agreement that the claim is assigned).[77] Another possibility, particularly in relation to certain types of claim such as receivables, is that the act of assignment is only effective as between assignor and assignee, and priority against third parties depends on registration. This, as we have already seen, is the approach under UCC–9, the PPSAs and the systems that they have influenced.[78] But in some other legal systems priority is defeasible and reversible. English law has this approach,[79] and, following it, the DCFR. If, in England,[80] Lorraine assigns to Magda and later to Norman, Magda has priority, because notification is not needed. But if Norman notifies first, priority is reversed. This rule is a priority rule, and not merely a rule for protecting debtors who act in good faith. For example, if Magda notifies Winnie (the debtor) the day after Norman notifies, and before Winnie has acted in reliance on Norman's notification, Norman still prevails over Magda. In the DCFR this rule is explained as part of the doctrine of good faith acquisition.[81]

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[74] K G C Reid, "Unintimated Assignations" 1989 SLT (News) 267 at 269. See also Anderson, *Assignation* paras 7-05 to 7-06.

[75] But Lena would be able to claim the money from Kevin. See Stair 4.40.33 and Scottish Law Commission, Discussion Paper on Recovery of Benefits Conferred Under Error of Law (Scot Law Com DP No 95, 1993) vol 1, para 3.59.

[76] Stair 4.35.7 expressed the view that there had to be a discernible gap of three hours between the intimation and the arrestment for one to have priority over the other, but as Anderson, *Assignation* para 6-37 states, under reference to *Wright v Anderson and Laurie* (1774) Mor 823, *Cameron v Boswall* (1772) Mor 821 and *Gibson & Balfour v Goldie* (1779) Mor 824, the better view is that priority can be by minutes and hours if the times can be clearly established.

[77] See eg German Civil Code arts 398 and 399; Swiss Civil Code art 164 and French Civil Code art 1323.

[78] See para 5.5 above. See eg the Security Interests (Jersey) Law 2012 s 29 and the UNCITRAL Model Law on Secured Transactions arts 1 (kk) and 29.

[79] Although, as discussed at paras 5.15–5.16 above there are proposals to reform English law to require registration of assignments of receivables for priority against third parties.

[80] Under the rule in *Dearle v Hall* (1828) 3 Russ 1. For discussion, see Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* paras 14.09–14.20.

[81] Cf Sale of Goods Act 1979 s 24. For criticism, see E Clive, "The Assignment Provisions of the Draft Common Frame of Reference" 2010 Juridical Review 275 at 282. See also, for discussion of a similar approach taken in

5.69 This approach tends to produce more complex cases than Scottish law. Take the following example,[82] assuming that the DCFR rules apply. Deirdre owes money to Chris. Chris assigns the claim for its repayment to Alastair on 10 May. He also, fraudulently, assigns to Aileen on 20 May. Aileen intimates on 25 May, and Alastair on 30 May. Under the DCFR rules, title passes to Alastair on 10 May, and then passes from him to Aileen on 25 May. What if Fraser, a creditor of Chris, arrests in the hands of Deirdre on 15 May? Then it would seem that Fraser prevails over Aileen (because he arrests before Chris assigns to her). But Aileen prevails over Alastair (because she notifies before he does). And Alastair prevails over Fraser (because when Fraser arrests, title has already passed from Chris to Alastair). Perhaps this priority circle could be resolved, but in the Discussion Paper we inclined to think that it was better to have a simple rule that priority is determined by priority of completion of title, and that this should be so regardless of *how* title is completed (with no external act, by means of intimation, by means of registration, etc). The rule would not be about the position of the debtor, which we deal with separately below.[83]

5.70 Almost all the consultees who responded to our question on this matter agreed that priority should continue to be determined simply by date of completion of title. This included the Faculty of Advocates, the Judges of the Court of Session and the Law Society of Scotland. Thus under our scheme if there are two competing assignations the assignee who is first either to intimate to the debtor or to register the assignation in the RoA would prevail. We are of the view that express provision is not required in the draft Bill because once an assignation is completed then it automatically follows that any competing assignation cannot be completed. If, in contrast, our policy were that a subsequent assignation in certain circumstances could trump an earlier one (as is the position under English law or under the DCFR) express provision would be required.

5.71 One final matter worth noting is that Scottish law, unlike English law does not recharacterise assignations (assignments) in security as security interests.[84] Like assignations other than for security purposes, they are *transfers*. Thus once a claim has been assigned in security to one assignee, it cannot be effectively assigned in security to a second assignee. There can be no "ranking" of assignations in security.

5.72 We recommend:

18. Priority of assignations should continue to be determined by time of completion of title.

Assignation subject to a condition

5.73 In certain transactions the parties wish to make an assignation subject to a condition, so that it does not take effect until that condition is satisfied. For example the parties may want to postpone the transfer of a claim to a *certain* date in the future rather than have transfer take place on intimation/registration. Sometimes it will be *uncertain* whether the

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the Principles of European Contract Law (PECL), a predecessor of the DCFR, G Lubbe, "Assignment" in H MacQueen and R Zimmermann (eds), *European Contract Law: Scots and South African Perspectives* (2006) 307–330.

[82] See also Discussion Paper, para 14.31.

[83] See paras 12.1–12.8 below.

[84] See generally Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* ch 4.

condition will ever be fulfilled. For example, the assignation might be conditional on the grant of planning permission or on the assignee getting married. The latter type of condition is traditionally referred to as a "suspensive condition".[85]

5.74 A suspensive condition can be contrasted with a "resolutive condition", the effect of which is to bring something to an end. Resolutive conditions in assignations only place an obligation on the assignee to re-assign (or "retrocess") the claim to the assignor if the condition is satisfied. The claim is not retrocessed automatically.[86]

5.75 It may be worth stressing that our concern here relates to a condition relating to the assignation. The claim itself may be the subject of a suspensive or resolutive condition. This matter is discussed later.[87]

5.76 While, in principle, suspensive conditions in assignations appear to be competent, the common law here is under-developed[88] and we understand that this has led to disputes in practice. We therefore asked consultees whether there should be legislative clarification of the effect of a suspensive condition in an assignation. There was support for this from most of the consultees who responded and universal support from the practitioner respondents. John MacLeod, however, argued that transfer subject to a suspensive condition was a general principle of property law and a rule in legislation for assignation might create doubt in relation to the transfer of other kinds of property.

5.77 Our view is that given the relative lack of authority in relation to assignation, a statutory rule would be helpful. This would confirm that an assignation may be made subject to a condition which requires to be satisfied before the claim is transferred. Such a condition might be suspensive but would not have to be. Thus it might relate to something happening which is certain to happen, or to a period of time elapsing during which something must not happen, for example the assignee failing to comply with certain obligations.

5.78 We have been informed that one of the disagreements in practice is whether the condition requiring to be satisfied can be written into a document other than the assignation itself. We consider that as the assignation is the conveyance it should require to go in the assignation document. It should be possible, however, for the condition to make reference to another document. Thus the assignation may be provided to be dependent on terms set out in a separate document being satisfied.

5.79 It may be that a debtor does not know that the condition has been satisfied (purified) and therefore performs to the assignor rather than the assignee. In such circumstances the debtor should be protected under the good faith rules set out in Chapter 12 below.

5.80 We recommend:

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[85] See eg Stair 1.3.7 ("the condition must necessarily be uncertain, either as being in the power of man's will, or as an accidental event"). See also H L MacQueen and J Thomson, *Contract Law in Scotland* (4th edn, 2016) paras 3.60–3.62.
[86] See Anderson, *Assignation* para 10-57.
[87] See paras 5.84–5.85 below.
[88] See Anderson, *Assignation* paras 10-55 and 10-56.

19. (a) It should be competent to make the assignation of a claim subject to a condition which must be satisfied before the claim is transferred. Such a condition could depend on something happening or not happening (whether or not it is certain that that thing will or will not happen) or on a period of time elapsing during which something must not happen (whether it is certain or not that the thing will happen at some time.)

(b) Any such condition should require to be specified in the assignation document.

(c) It should be permissible for the specification to include reference to another document the terms of which are not reproduced in the assignation document.

(d) The claim should not transfer until the condition is satisfied.

(Draft Bill, ss 2 and 3(1) & (2)(d))

Assignation of future and contingent claims

General

5.81 Due to the requirement of intimation, it is impractical under the current law to assign claims which do not yet exist at the time the assignation is granted. Thus imagine that a business assigns its future invoices to a financing company. As regards each invoice, the assignation is only effective upon the invoice being issued and there being intimation to the individual customer. This is cumbersome. Where intimation is not required, as is the case under other legal systems and international instruments, the assignation of as-yet non-existent claims is facilitated. But the area is a difficult one both conceptually and in policy terms.

5.82 Before going any further, we need to say something about terminology. This is best done by means of examples. Say Ann owes Bernie £10,000 but the debt is not repayable until 2020. This is a claim which already *exists*, albeit payment cannot be demanded until 2020.[89] Bernie could assign to Colin and Colin could complete the assignation today by intimating to Ann. But Ann's obligation to repay can be referred to as a "future obligation" since it is not until 2020 that she must perform.[90] And in turn the claim might be described as a "future claim" because performance is not required until a future date. Despite this, the assignation of the claim to Colin does not present particular difficulties because intimation can be made to Ann. Both she as debtor and the claim itself are readily identifiable.

5.83 Contrast the following. A plumbing company assigns its invoices present and future to a factor on 1 February. On 1 March the company carries out work for Mrs Jones and bills her. At the time of the assignation nothing was owed by Mrs Jones. No work had been

[89] In the words of Stair 1.3.7: "But obligations to a day as such as are presently binding, but the effect or execution thereof is suspended to a day."

[90] MacQueen and Thomson, *Contract Law in Scotland* para 3.60; W M Gloag and R C Henderson, *The Law of Scotland* (14th edn, by Lord Eassie and H L MacQueen, 2017) para 3.12.

carried out for her. There was no claim and indeed no identifiable debtor. Through the lens of the assignation such a claim can be described as a "contingent claim".[91] It depends on the work being carried out for Mrs Jones. Thus the work may have been to carry out a repair to her shower. But for her shower breaking no work would have been needed and there would have been no invoice. Given that the claim does not arise until after the assignation, it is also possible to refer to such a claim as a "future claim". This is the approach which was taken in the Discussion Paper under reference to the DCFR[92] and indeed by a number of Scottish commentators.[93] In this Report, however, we do not use the term in this way because of the potential for confusion with future obligations, as described above.

5.84 A further example of a contingent claim is a claim which is the subject of a suspensive condition. For example, Gordon promises to give Harriet £1,000 if she gets a place on a particular university course. Harriet assigns her right to Ian, to whom she is indebted. The claim only arises if Harriet obtains the place. Only then can it be transferred to Ian.

5.85 The position as regards resolutive conditions is different. Suppose that the Ann/Bernie contract referred to above had this clause: "But Ann's obligation to repay shall be extinguished if, before 2020, Ann dies." The claim is still assignable but if Ann dies before 2020 Colin will be owed nothing from Ann's estate under the *assignatus utitur jure auctoris* rule.[94] Ann's obligation relates to her contract with Bernie and not the transfer of Bernie's claim to Colin by means of the assignation which is effective immediately.

5.86 Another example familiar in practice of a contingent claim is an unvested right under a will or trust. Thus Nicola may be entitled to a sum of money as a beneficiary under a will if she survives the testator by six months. The right remains unvested until the six months passes. But it may be that the right can be assigned by intimation to the executor and this case is less problematic than the assignation of a claim which does not yet exist.[95]

5.87 It is of course possible to contract to sell a contingent claim, in the same way as a baker might contract to sell a birthday cake that has not yet been baked. Similarly, copyrights which do not yet exist (because, for example, the relevant book has not yet been written or relevant picture has not yet been painted) are commonly assigned.

Accretion

5.88 Under the current law it is arguable that an assignation of a claim which does not exist at the time that the assignation is granted can be completed by a doctrine known as accretion. It provides that if X ostensibly conveys to Y a right that X does not have, but X subsequently acquires that right, the right will at that stage pass immediately and automatically without the need for any further act of transfer, from X to Y.[96] In determining

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[91] See generally G L Gretton, "The Assignation of Contingent Rights" 1993 Juridical Review 23.
[92] See Discussion Paper questions 15 and 16; DCFR Book III and Commentary, p 1027.
[93] See S Mills, N Ruddy and N Davidson, *Salinger on Factoring* (5th edn, 2017) para 7-49 (R B Wood); Anderson, *Assignation* paras 11-52 to 11-53 and A McAlpine, "Raising Finance over Claims to Payment" 2015 Juridical Review 275.
[94] See paras 12.27–12.32 below.
[95] See Gretton, "The Assignation of Contingent Rights" (n 91 above).
[96] On accretion generally see Reid, *Property* paras 677-679. For the applicability of the doctrine to assignations see Anderson, *Assignation* ch 11.

whether it can apply to assignation, we noted in the Discussion Paper that different types of case must be distinguished.[97]

5.89 The first type of case is where a claim exists against Z and is assigned by X to Y, who intimates to Z. But X was not in fact the holder of the claim. The holder was A. The assignation is therefore ineffective. But if A later assigns to X, then Y's title will be validated by accretion.[98] Of course, cases of this sort are unusual.

5.90 Whereas in the first type of case the claim existed, but was assigned by the wrong party, in the second type of case the claim does not exist at the time of the ostensible assignation. J assigns to K a claim that does not exist. This possibility itself sub-divides into two sub-cases.

5.91 The first sub-case is where the identity of the account party is not known and so no intimation is made. Here accretion cannot operate. An essential requirement of accretion is that the original transfer is fully valid in all respects *except* that the granter has no title. But if there is no intimation, there is not even a *purported* transfer.[99]

5.92 The second sub-case is where a good guess can be made as to the identity of the account party. For example, a company, J, often sells goods to a buyer, L. J assigns its claims against L in favour of K. Intimation is made to L, in respect of claims that it does not yet owe but may hereafter owe. If, later, a debt does arise, owed by L to J, does accretion operate so as to validate the assignation? Whereas the law is clear in the first sub-case (above), it is not so clear in this second sub-case.[100] We inclined to the view in the Discussion Paper that an assignation of a claim which does not yet exist cannot be completed by accretion on the basis that at the time intimation is made the person to whom it is made is not the account party.[101] This is all unsatisfactory for commerce, which desires certainty and the ability to assign claims arising subsequent to the granting of the assignation.

Reform

5.93 The current law in Scotland in relation to the assignation of claims arising after the assignation is granted contrasts unfavourably with the position in England and Wales, and elsewhere, where such assignations (assignments) are competent in equity.[102] Clearly our earlier recommendation that registration should become an alternative to intimation for completion of an assignation should assist matters. But if we were to recommend that the details of not only the assignor and assignee, but also the account debtor, should be

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[97] Discussion Paper, paras 4.60–4.63.
[98] Y's title would also be validated if A were to convey to Y.
[99] *Buchanan v Alba Diagnostics Ltd* 2004 SC (HL) 9 has *dicta* about accretion in relation to assignations of intellectual property rights. But these dicta seem to overlook the fact that accretion cannot operate unless there has been a purported transfer. See R G Anderson, "*Buchanan v Alba Diagnostics*: Accretion of Title and Assignation of Future Patents" (2005) 9 EdinLR 457.
[100] Cf *Bank of Scotland Cashflow Finance v Heritage International Transport Ltd* 2003 SLT (Sh Ct) 107, on which see the Discussion Paper, para 4.63.
[101] Discussion Paper, para 4.65.
[102] *Tailby v Official Receiver* (1888) 13 App Cas 523.

registered then the scope for assignation of future rights would remain limited. We do not recommend this.[103]

5.94 We drew attention in the Discussion Paper to the relevant DCFR provision. It provides that "a future right to performance may be the subject of an act of assignment but the transfer of the right depends on its coming into existence and being identifiable as the right to which the act of assignment relates."[104]

5.95 Accordingly we asked consultees whether the law should allow a future claim[105] to be assigned (subject to the right in due course coming into being and being identifiable as the claim to which the assignation relates). All the consultees who responded to this question agreed. The WS Society said that this is "the single reform of the law which is probably the one most fundamentally required to make Scots law a usable system for invoice finance and securitisations." ABFA said that because of the current law "much of the Scottish business [carried out by our members] is artificially channelled through English law to avoid Scots law difficulties." Brodies and the Law Society of Scotland said that the reform would "greatly facilitate security arrangements in respect of for example multi-let investment properties and securitisations of trade and autoloan receivables."

5.96 As well as the claim coming into being and being identifiable as the claim to which the assignation relates it must be necessary of course for the assignor to become the holder for otherwise it cannot be transferred by the assignation.

5.97 We therefore recommend:

20. It should be competent to assign a claim which does not exist at the time that the assignation document is granted, but for the claim to be transferred it should require to have come into being and be held by the assignor.

(Draft Bill, ss 1(5) and 3(2)(a))

5.98 In practice we expect that invoice financing would almost always proceed by means of registration. This is because it is invariably of claims arising subsequent to the assignation and therefore the details of account debtors are not known. Intimation is not possible.[106] The RoA would therefore be a near-definitive source of information as to whether invoice financing has taken place.

5.99 We mentioned above the uncertainty as to whether the doctrine of accretion was relevant to the assignation of claims which arise subsequent to the assignation. We

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[103] See Chapter 7 below.

[104] DCFR III.–5:106. See also French Civil Code art 1323(3): "Toutefois, le transfert d'une créance future n'a lieu qu'au jour de sa naissance, tant entre les parties que vis-à-vis des tiers." (However, the transfer of a future right takes effect only on the day when it comes into existence, as between the parties and as regards third parties.)

[105] In the sense of a claim that is not in existence when the assignation is granted. Cf para 5.80 above.

[106] Until the debtor becomes known, but intimation made at that point may not be sufficient to achieve priority, in particular where the assignor has become insolvent. See N O Akseli, "The United Nations Convention on the Assignment of Receivables in International Trade and Small Businesses" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 465 at 478–479.

consider that the law should be made clear and that it be provided that it has no application here.

5.100 We recommend:

21. In relation to the transfer of claims which arise after the assignation document is granted, any rule of law as to accretion should be disregarded.

(Draft Bill, s 3(3))

Restriction in respect of wages or salary where assignor is an individual

5.101 In the Discussion Paper, we noted that there are existing statutory provisions preventing the assignations of pensions and social security rights.[107] We asked whether there should be a general restriction on the ability of consumers to assign future rights.[108] In the context of reforming the law to make it easier to assign future rights, our concern was whether greater protection for consumers was required. A restriction on the ability of consumers to assign future rights was generally supported by consultees. But several law firms commented that care should be taken not to interfere with financial planning transactions where, for example, contingent rights under wills and trusts are assigned.

5.102 We have therefore decided to recommend a more limited rule to prevent individuals from assigning their salary or wages.[109] People should not be able to assign away their core income. Attempting, however, to make clear definition in this regard is not easy. There is a comprehensive definition of "wages" in section 27 of the Employment Rights Act 1996, but as a matter of general usage the term is not applied in relation to payments to officeholders such as Ministers and judges. We consider, however, that it would be helpful to draw on section 27 in part to make it clear that related income, namely fees, bonuses, commissions, holiday pay and other emoluments are to be included in the prohibition.[110] On one view, these go beyond core income but we are minded to take a wider rather than narrower approach. Existing statutory restrictions on the assignation of income would also continue to apply,[111] including the prohibitions in relation to pensions and social security payments. In addition, however, we consider that the new prohibition should also apply to expenses payable to the individual in relation to the individual's employment and redundancy payments.[112]

5.103 We recommend:

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[107] Discussion Paper, paras 18.40–18.41. See the Pensions Act 1995 s 91 and Social Security Administration Act 1992 s 187. See generally Anderson, *Assignation* para 10-30.
[108] Discussion Paper, para 14.68.
[109] For a broadly similar rule in relation to the granting of security, see the DCFR IX.–2:107. See too the Dutch Civil Code art 7:633(1).
[110] Employment Rights Act 1996 s 27(1)(a). Much of the rest of the definition concerns social security payments, an area in which some provision has already been made. See para 5.92 above.
[111] For example, the Merchant Shipping Act 1995 s 34.
[112] Notwithstanding the Employment Rights Act 1996 s 27(2). The question of whether "expenses" was included within the definition of salary and wages was raised by R3 in their response to our draft Bill consultation in July 2017.

22. (a) Individuals should be prohibited from assigning a claim in respect of wages or salary, including any fee, bonus, commission, holiday pay or other emolument referable to their employment, or to expenses or a redundancy payment.

(b) This rule should be without prejudice to any other enactment.

(Draft Bill, s 8)

5.104 We also gave careful consideration as to whether such protections should be extended to sole traders to prevent them from assigning future invoices (perhaps below a certain threshold). This was a matter which we found difficult. There is arguably little difference between an employee plumber with a spouse and family, and a sole trader plumber with a spouse and family. Both require income to support them. We discussed the issue in some detail with our advisory group and with insolvency experts. The difficulty with such a rule is that sole traders would be debarred from using invoice financing, which we understand can be of great commercial benefit to them. We think that a threshold provision (for example, a sole trader could not assign in any year the first £25,000 of invoices issued) would be too complex to operate.[113] In practice we were told that invoice finance providers would not enter into an arrangement under which someone assigned away all their future invoices. And in cases where someone was duped to do so, common-law remedies such as fraud and undue influence could be invoked. We have therefore concluded against extending the prohibition to sole traders.

Assignation of subsequently-arising claims and commencement of insolvency

5.105 There remains to be discussed the issue of the effect of the assignor's insolvency on the assignation of a claim which comes into existence subsequent to the grant of the assignation. In the Discussion Paper we noted the DCFR provision that: "an assignment of a right which was a future right at the time of the act of assignment is regarded as having taken place when all requirements *other than those dependent on the existence of the right* were satisfied."[114] The commentary to that provision notes: "The main policy reason behind the rule . . . is that in the case of an act of assignment of future rights, the assignee, who will very often have paid for the rights, should be preferred to the creditors of the assignor."[115] Nevertheless, this seems to involve re-writing the past. For example, X assigns to Y an as-yet-non-existent claim against Z on 1 May. The claim comes into existence on 1 November. The provision just quoted seems to mean that Z is deemed to have owed the money to Y as from 1 May.[116] We thought that this was unsatisfactory. We therefore asked consultees whether they agreed that the transfer of a claim should not be deemed to take place before the claim comes into being.

5.106 Consultees generally agreed. The Law Society of Scotland, however, also made the valuable point that problems will arise in the event of the supervening insolvency of the assignor and that a rule should be formulated in relation to that. Insolvency law is a huge

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[113] For example, the net income to the sole trader from the gross invoice will vary from case to case.
[114] DCFR III.–5:114.
[115] DCFR Commentary, p 1053.
[116] Cf DCFR IX.–4:101 which allows security rights to have a priority that is *earlier than their creation*. This approach derives from UCC–9/PPSAs.

and complex area as regards which this project has generally taken the approach that it is outwith its scope.[117] We therefore did not consult on insolvency law in the Discussion Paper. This leaves a difficulty in formulating the rule as to the effect of insolvency on the assignation. We have been assisted in this regard by our advisory group and insolvency experts.

5.107 As a result of these discussions, we have concluded that the assignation of certain subsequently-arising claims should not be rendered ineffective as a result of the claim coming into being after the commencement of an insolvency process. There should be a direct rule to this effect, rather than the fictional back-dating of the DCFR. The types of claims which we consider should continue to be transferred to the assignee should be claims to income deriving from property. For example, if someone assigns the future royalties from a patent or the future rents under a lease, the assignation should continue to be effective. But this rule should not apply to any income attributable to anything agreed to by, or done by, the assignor after the assignor becomes insolvent. For example, if John is a self-employed chauffeur with a limousine who assigns future invoices in respect of driving jobs, any invoices in respect of jobs carried out after he is sequestrated would not be assigned. While these derive from the use of his vehicle, they required work, namely driving, on his part. In a similar vein, claims in respect of income from property which is not existence at the time the assignor became insolvent should not be transferred. For example, Joan assigns the royalties from her books. She writes a new book after she becomes sequestrated. The royalties from that book would not transfer.

5.108 There are many different types of insolvency (and similar) processes both within Scotland and elsewhere. Moreover, there are variations within some of the processes. For example, not all liquidations are "insolvent liquidations". Deciding on exactly which processes should be subject to the above rules is not an easy matter, not least without the benefit of formal consultation. We have therefore included in our draft Bill a relatively comprehensive list of Scottish processes.[118] But we have given the Scottish Ministers the power to amend the provisions by secondary legislation, for example to add further cases such as equivalent processes in other jurisdictions. We would expect the Scottish Government to consult specifically on this matter as part of any future consultation on this Report.

5.109 We recommend:

23. (a) An assignation granted before the assignor becomes insolvent should be ineffective as regards a claim if the assignor is insolvent at the time of becoming the holder of the claim.

(b) An assignor who is an individual, or the estate of which may be sequestrated, becomes insolvent when:

(i) the assignor's estate is sequestrated,

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[117] See para 1.26 above.

[118] We have included only administrative receiverships as receiverships over only a part of the assignor's property are different in nature to an insolvency process.

(ii) the assignor grants a trust deed for creditors or makes a composition or arrangement with creditors,

(iii) a voluntary arrangement proposed by the assignor is approved, or

(iv) the assignor's application for a debt payment programme is approved under section 2 of the Debt Arrangement and Attachment (Scotland) Act 2002.

(c) An assignor which is not an individual becomes insolvent when:

(i) a decision approving a voluntary arrangement entered into by the assignor has effect under section 4A of the Insolvency Act 1986,

(ii) the assignor is wound up under Part 4 or 5 of the 1986 Act or under section 367 of the Financial Services and Markets Act 2000,

(iii) an administrative receiver, as defined in section 251 of the 1986 Act, is appointed over all or part (being a part which includes the claim) of the property of the assignor, or

(iv) the assignor enters administration, ("enters administration" being construed in accordance with paragraph 1(1) and (2) of schedule B1 of the 1986 Act).

(d) The above rule should not apply as regards a claim in respect of income from property but only in so far as the claim:

(i) is not attributable to anything agreed to by, or done by, the assignor after the assignor becomes insolvent, and

(ii) relates to the use of property in existence at the time the assignor became insolvent.

(e) The Scottish Ministers should have power to amend the definition of "insolvent".

(Draft Bill, s 5(1) to (4), (7)(a) & (8))

Effect of discharge in sequestration etc

5.110 The above rules deal with the effect of the *commencement* of an insolvency process on the assignation of a claim arising subsequent to the assignation. There is also the question of what is to happen after the end of an insolvency process. In the case of a winding up (liquidation) the assignor company will cease to exist so it can no longer hold any claims, future or otherwise. In practice, we understand that administrations and receiverships typically end in a winding up, although not always. The question is most

pressing as regards a sequestration. A sole trader may have assigned certain claims, for example, in respect of sums due by customers for certain types of services, in all time coming. It does not seem appropriate that this assignation should survive the trader's discharge following a sequestration. We consider that the assignation should be ineffective as regards claims which come into being following the discharge. The effect of this rule, coupled with the rule outlined above, is that an assignation of royalties or rents while remaining good despite the assignor being sequestrated, would not carry any royalties or rents arising post-discharge. At that point the assignor would have a completely fresh start.

5.111 We think that a similar rule should apply to protected trusts deeds and that the Scottish Ministers should also have the power to make regulations to apply the rule to other insolvency processes. Again we would expect there to be consultation on this issue as part of the consultation on this Report.

5.112 We recommend:

24. (a) Where a person who has assigned a claim in whole or in part is discharged following either sequestration or the granting of a protected trust deed the assignation should be ineffective as regards the claim (or part) to which it relates if, as at the time of discharge, the claim has not come into being.

(b) The Scottish Ministers should have the power to amend the above rule to apply it to other insolvency processes.

(Draft Bill, s 5(5), (6) & (7)(b))

Chapter 6 Register of Assignations: general

Introduction

6.1 In this chapter we make recommendations in relation to the establishment, management and nature of the new Register of Assignations (RoA). It would be the register in which assignations of claims could be registered. An important matter is what exactly is to be registered and, for reasons which we set out below, we recommend document registration. We consider too that the RoA should be electronic and for the most part automated.

Establishment of the RoA

6.2 In the Discussion Paper we suggested that registration should be (i) an optional alternative to intimation as a method of transferring claims; and (ii) the method by which a new security right over moveable property (called the "statutory pledge" in this Report) would be created.[1]

6.3 The Discussion Paper went on to propose that a new public register should be established for these purposes, provisionally to be called the Register of Moveable Transactions (RMT). This proposal had the general support of consultees, although understandably some said that this was subject to their comments on other questions in the Discussion Paper. Naturally those such as John MacLeod and Scott Wortley, who did not support registration of assignations, made that point once again. They accepted, however, that if the policy decision was to have registration, then the RMT would be the appropriate place for this. Dr Ross Anderson advocated a different approach of registration in the Books of Council and Session.[2] After due reflection, however, we concluded that it is preferable to make provision for a new register which can best deliver our recommendations on searching etc rather than to try to adapt an existing register which is used far more widely than for moveable transactions.

6.4 As we worked on the draft legislative provisions which would establish the new register it became clear that the assignation and the statutory pledge parts of the register would have significant differences between them. For example, only assignations would be registrable in the assignations part. An assignation as a *transfer* or event is a one-off transaction. It requires a single registration. In contrast, a statutory pledge involves the creation of a new *right* which can be transferred, varied or extinguished. The register must be able to take account of such juridical acts and therefore must be more complex.

6.5 The approach under UCC–9 and the PPSA systems is rather different. One register is used in which typically (a) any transaction which functions as a security and (b) outright

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[1] Discussion Paper, para 20.1.

[2] See R G Anderson and J W A Biemans, "Reform of Assignation in Security: Lessons from the Netherlands" (2012) 16 EdinLR 24 at 36 and R G Anderson, "A Critique" (2012) 16 EdinLR 267 at 269–270. But, as noted at para 5.8 above, Dr Anderson subsequently favoured not requiring registration.

assignments of receivables are registrable.[3] This form of registration is notice filing and registration is only needed to achieve priority against third parties. For the reasons set out below in Chapter 18 we do not recommend notice filing or a functional approach to security rights. Nor do we recommend relative effectiveness.[4] In addition, registration in the RoA would be available for any claim (as defined)[5] and not only receivables. As a consequence, our approach can be seen to contrast materially with that of UCC–9 and the PPSAs.

6.6 We have reached the conclusion therefore that it would be preferable to have two separate registers. The result of this approach is that the relevant draft Bill provisions on (1) registration of assignations and (2) registration of statutory pledges are separated. We think that this will make matters easier for the reader of the legislation. It would even enable the assignations reforms to be taken forward separately from our recommendations on security over moveable property which we set out in volume 2 of this Report.

6.7 For assignations, we think that the register should be known as the Register of Assignations (RoA). We therefore recommend:

25. A new public register should be established, to be called the Register of Assignations, in which assignations of claims can be registered.

(Draft Bill, s 19(1))

Management of the RoA

6.8 The obvious candidate for the management of the RoA is the Department of the Registers of Scotland, which is already responsible for eighteen Scottish registers, notably the Register of Sasines, the Land Register and the Books of Council and Session. In the Discussion Paper, however, we said that it made sense to follow the flexible approach taken for the Register of Community Interests in Land.[6] That register must be kept by the Keeper of the Registers of Scotland or by such other person as the Scottish Ministers may appoint. This proposal had strong support from consultees.

6.9 We have subsequently had detailed discussions with Registers of Scotland as to the establishment of the register. As a result of this we are convinced that the Keeper is best placed to manage the register rather than any other person and that a more flexible approach is unnecessary.[7]

6.10 We therefore recommend:

26. The register should be under the management and control of the Keeper of the Registers of Scotland.

(Draft Bill, s 19(2))

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[3] See eg UCC § 9-202; NZ PPSA 1999 s 17; Security Interests (Jersey) Law 2012 s 4 and UNCITRAL Model Law on Secured Transactions art 2(kk).
[4] See para 5.17 above.
[5] For the definition of "claim" see above paras 4.9–4.13 above.
[6] Land Reform (Scotland) Act 2003 s 36(9).
[7] This mirrors the position as regards the Land Register. See LR(S)A 2012 s 1(2).

Costs

6.11 The RoA, like the Land Register and other registers under the Keeper's control, should be self-financing. It should not be a burden on the taxpayer. Clearly, there would be start-up costs. Registers of Scotland have estimated that in total for the RoA and the new Register of Statutory Pledges these would be around £500,000 to £1m.[8] Such costs would be recouped from future income generated by the registers. The income would consist mainly of (i) registration fees and (ii) search fees. In UCC–9/PPSA jurisdictions these fees are relatively modest because of the number of registrations and the fact that the register is automated.[9] We return to the subject of automation later.[10] The number of registrations in the RoA would be lower than under a UCC–9/PPSA system, because only assignations of claims would be registered. Nevertheless, we believe that the frequency of registrations would still allow the start-up costs to be repaid within a relatively short period, without high fees for registration and searching being required.[11]

Not a title register

6.12 A title register in principle allows someone checking it to determine who has the ownership of an asset. The best Scottish example is the Land Register.[12] Needless to say, title registers are not infallible. The information in them can be inaccurate. Nevertheless, their purpose remains to identify ownership.[13] The RoA in contrast would not be a title register. It would only be a register of assignations of claims.[14] The fact that Neil has assigned a claim in favour of Orinoco and that this assignation has been registered in the RoA would not confirm that Neil has title to the claim. Nor would the fact of registration of itself mean that Orinoco would acquire title.[15] In practice of course it is likely that Neil does hold the claim as people do not usually assign the claims of others. But that is only a matter of fact.

What is to be registered?

6.13 The Discussion Paper canvassed in some detail what type of registration should be made.[16] Essentially, it identified two possibilities (i) notice filing and (ii) transaction filing, by means of registering the assignation (or security) document. We discuss the differences between these in the following paragraphs, but it may be helpful first to quote a short summary from one of our previous publications which has been drawn on internationally:

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[8] This is broadly in line with the US $1,180,300 which it cost to establish the NZ PPSR in 2002. See Law Com Report No 296 para 2.9 fn 11.

[9] For example, in New Zealand the fee is currently NZ$20 (about £11). See http://www.ppsr.govt.nz/cms/customer-support/fees. In Australia the fees vary depending on the time-period of the registration chosen. For a registration of up to 7 years the fee is A$6.80 (about £4). See https://www.ppsr.gov.au/fees.

[10] See paras 6.39–6.44 below.

[11] See further the BRIA for this Report, available on our website.

[12] See Reid and Gretton, *Land Registration* para 1.13.

[13] And of course subordinate rights held over the property which require to be registered, such as standard securities.

[14] Or, more precisely further to our recommendations later in this Chapter, a register of assignation documents.

[15] There would no Keeper's "Midas touch" as there was under the Land Registration (Scotland) Act 1979. See Gretton and Steven, *Property, Trusts and Succession* para 7.77.

[16] Discussion Paper, paras 20.8–20.20. While the discussion was made in the context of the new security right, the same principles apply to assignation.

> "The most characteristic difference between notice filing and traditional systems of registration is that notice filing is parties-specific rather than transaction-specific. What is filed are not the details of a particular security but notice that certain parties have entered into, or may in future enter into, a secured transaction in relation to specified property. This approach has certain implications. A notice may be filed in advance of the transaction and the proposed transaction may never take place. The same notice may serve a series of connected transactions. And the information given on the register is necessarily rather general in character, being an invitation to further inquiry rather than a full account of the right in security."[17]

Notice filing

6.14 This is the registration system used under UCC–9 and the PPSAs. Under this system it is not a security right (normally referred to as a "security interest" and which includes certain assignments[18]) itself that is registered. Rather it is only notice of it.[19] The notice is given by means of a brief financing statement, which can be registered before or after the security interest is granted. The security interest is created (or, to use the technical language, "attaches") off-register but is given third party effect (is "perfected") by registration. It is possible for a notice to be filed and no security interest ever to be granted. Therefore the register is not definitive as to whether a security interest has been granted, in contrast to the position for transaction filing.[20]

6.15 Under a notice filing system there are two documents: the security contract and the financing statement. Only the latter is registered. This gives rise to the possibility of discrepancy between the two. But the same may be said to be true under an approach where the security document is registered, because there may still be a preceding contractual document which the security document does not properly reflect, for example if the description of the encumbered property is wrong.

6.16 The brevity of a financing statement means that it can be completed very easily online by the secured creditor, with drop-down menu options, for example in relation to asset classes. On the other hand, the minimal nature of the information means that there require to be rules to allow parties with a legitimate interest to ascertain the extent of what is encumbered. Thus the financing statement might state "goods: livestock"[21] but there might only be a security interest over cattle or ostriches. Having to make enquiries is to some extent inconvenient and also has cost implications.

6.17 At the core of the UCC–9/PPSA approach is the idea that failure to register does not mean that the security interest fails. It is merely unperfected. In a question with the provider it is effective and can be enforced. Indeed in New Zealand it is also effective on the

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[17] Scottish Law Commission, Discussion Paper on Registration of Rights in Security by Companies (Scot Law Com DP No 121, 2002) para 1.26 quoted eg in Allan, *The Law of Secured Credit* 447 and I Otabor-Olubor, "Reforming the law of secured transactions: bridging the gap between the company charge and CBN Regulations security interests" (2017) 17 Journal of Corporate Law Studies 39 at 51.

[18] See para 5.5 above.

[19] In addition to the sources mentioned in the Discussion Paper see Hamwijk, *Publicity in Secured Transactions Law* and the Secured Transactions Law Reform Project Discussion Paper of January 2017 by Professor Louise Gullifer, available at https://stlrp.files.wordpress.com/2017/01/gullifer-registration.pdf.

[20] See R Calnan, "What makes a good law of security?" in F Dahan (ed), *Research Handbook on Secured Financing in Commercial Transactions* (2016) 451 at 477.

[21] We use this example from New Zealand. See http://www.ppsr.govt.nz/cms/secured-party-information/financing-statements/what-you-need-to-know/collateral.

provider's insolvency.[22] But as against other secured creditors who have registered, it is ineffective. In contrast the Scottish approach to property rights is that they are not created without an external act, such as registration. Moreover, the idea of a right in property being created which is effective against some parties (for example the assignor) but not others (for example, the assignor's creditors) conflicts with the general approach of Scottish property law and its dislike of "limping" rights.[23]

Transaction filing

6.18 Under a transaction filing system it is not notices of (possible) security rights which are registered. Rather, it is an actual security right. The registration is specific to the creation of that security right. It is therefore not possible for the same notice to cover several security rights. And generally registration takes place after the parties have entered into the transaction and not before (although it is possible to have an advance notice system).

6.19 The Discussion Paper favoured transaction filing by means of registration of the constitutive document of the new security right (the statutory pledge).[24] Reference was made to Form B standard securities where a relatively short-form document is registered and the details of the loan etc are kept off-register and therefore confidential. The Discussion Paper did not directly ask a question about registration of the assignation document, but it clearly contemplated this type of registration for such documents too.

6.20 There was strong support from consultees for registration of assignation documents.

Developments

6.21 Since consultation closed, there have been several significant developments. First and most importantly, with effect from 1 April 2013, the company charges registration scheme in Part 25 of the Companies Act 2006 was reformed.[25] Formerly, what had to be registered were "particulars" of the charge, rather than the charge document. Now, it is a certified copy of the charge document (instrument) itself.[26] We understand that this change has been widely welcomed by stakeholders because it has removed the need to describe the encumbered property and secured obligation.[27] Instead the document can be relied on to provide this information. It is possible for certain parts of the document to be redacted: (a) personal information relating to an individual (other than the individual's name); (b) the number or other identifier of a bank or securities account of a company or individual; and (c) a signature.[28] The reasons are to protect confidentiality and to reduce the possibility for fraud.

6.22 We discussed the 1 April 2013 changes with our advisory group and they were supportive of them. They considered, in agreement with consultees, that a copy of an assignation document should require to be registered in the RoA and that the detail to be

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[22] See Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 8.
[23] See para 5.17 above.
[24] Discussion Paper, paras 20.16–20.20.
[25] Companies Act 2006 (Amendment of Part 25) Regulations 2013 (SI 2013/600). See K G C Reid and G L Gretton, *Conveyancing 2013* (2014) 172-178 and H Patrick, "Charges changing" 2013 JLSS Feb/20.
[26] Companies Act 2006 s 859A(3).
[27] There is a very basic tick box system on the application form in respect of certain asset classes.
[28] Companies Act 2006 s 859G.

included in the application form for registration (which we discuss in the next chapter) should be limited, so as to avoid the possibility of mistakes. They were also of the view that redaction should be allowed in a similar way as is allowed under Part 25 of the Companies Act 2006. Finally, it was noted that having a document registration system would help facilitate an information-sharing order under section 893 of the Companies Act 2006.[29]

6.23 The second development was the enactment of the Belgian Pledge Act of 11 July 2013.[30] This effects a major recasting of the law on security over moveables in Belgium. While a functional approach is chosen and the DCFR Book IX is influential, the form of registration is not notice filing in the UCC–9/PPSA sense. Rather, relevant data in relation to each security transaction has to be registered by means of an online form.[31] But the constitutive document is not registered. Indeed, no document is required except where one of the parties is a consumer.[32] An advantage of this approach is that confidential information in the security agreement is kept off the register. The register is also technically simpler because it contains no documents, only data. On the other hand there are disadvantages as regards transaction costs commonly associated with notice filing, such as potentially greater time and costs in obtaining off-register information. We highlighted the Belgian approach to our advisory group, but they continued to favour a document registration approach, familiar to them both for standard securities and under Part 25 of the Companies Act 2006 where confidential information is kept off the register by means of short documents or redaction.

6.24 The third development was the publication in 2014 of the UNCITRAL Guide on the Implementation of a Security Rights Registry, which should now be read with the UNCITRAL Model Law on Secured Transactions of 2016. The Guide sets out four advantages of notice filing over document filing.[33] These are: (1) it reduces transaction costs both for registrants (as they do not need to register the security agreement) and for searchers (as they do not need to peruse potentially voluminous documentation); (2) it reduces the administrative and archival burden on registry system operators; (3) it reduces the risk of registration error because the less information that must be submitted the lower the risk of error and (4) it enhances privacy and confidentiality because the information on the register is minimal.

6.25 In the context of the functional approach to security rights taken by UNCITRAL these arguments seem strong. The scope for increased costs and risks of error appears great where every transaction that functions as a security has to be registered. The idea of a register full of sale of goods contracts (with retention of title clauses) and hire-purchase agreements is unpalatable. In contrast the RoA would have a far narrower scope: only assignations of claims. The documentation and registration would normally be handled by solicitors and the risk of registering the wrong document should be slight. Moreover, Registers of Scotland have informed us that a facility for documents to be registered as well as data is technologically not problematic. We have discussed the transaction costs and confidentiality issues above.

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[29] See Chapter 36 below.

[30] See E Dirix, "The Belgian Reform on Security Interests in Movable Property" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 391–404. The legislation is due to be brought into force on 1 January 2018.

[31] Dirix (above at 399) sees this as "an intermediate step between 'transactional filing' and 'notice filing'".

[32] Belgian Pledge Act of 11 July 2013 art 9 (which provides for art 4 of the new Book III title XVII of the Civil Code).

[33] UNCITRAL Guide on the Implementation of a Security Rights Registry para 59.

6.26 The fourth development was the statutory review of the Australian PPSA 2009, which was published in 2015. It is possible for the security agreement to be uploaded to the Australian PPSR, but this is rarely done. The reviewer was asked to consider whether it should be mandatory to register the agreement. He concluded that it should not be because (1) it would impose additional burdens on the parties because not only the original agreement would have to be registered, but so too would amendments; (2) the agreement will not necessarily disclose exactly what the encumbered property is; and (3) there may be confidential terms in the document.[34] Once again these arguments are strong in a functional security context. In relation to the first point, an assignation which has taken effect as a transfer cannot be amended.[35] While the second point is of course true, registration of the assignation document means that it is not essential for a description to be provided in a data box in the application for registration. We have considered the third point, confidentiality, already.

6.27 Finally, we would mention the Draft Secured Transactions Code of the Financial Law Committee of the City of London Law Society, the latest draft of which was published in July 2016. It favours document registration based on the Companies Register approach since 1 April 2013.[36] In contrast a Discussion Paper of the Secured Transactions Law Reform Project of January 2017 sees advantages in notice filing.[37]

Conclusion

6.28 We have concluded that the assignation document should require to be registered. The RoA would therefore be more precisely a register of assignation documents.[38] As under Part 25 of the Companies Act 2006 we think that it should be possible for a copy of the document to suffice, such as a scanned copy. But, following discussions with our advisory group, we have been persuaded that there is not a need for the document to be certified. Someone who is willing to forge a document is likely to be willing to add a false certification and it is not clear that fraud is deterred by such a requirement. It may be, however, that certification would be required to enable an information-sharing order under section 893 of the 2006 Act and certainly it should be possible for the Scottish Ministers to impose such a requirement under rules. Such rules might also make it a condition of making an application that the applicant is certifying that the copy submitted is a true one. We think that rules should also be able to allow redaction as is the case under Part 25 of the 2006 Act.[39]

6.29 The document would be registered along with an application which would provide brief data which would go into the entry on the register. We discuss that data in the next chapter.

6.30 We recommend:

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[34] Australian Statutory Review 2015, para 6.11.2.
[35] Of course it would be possible to carry out a retrocession of any claim transferred in error, but that is another transfer rather than an amendment.
[36] City of London Law Society draft Secured Transactions Code section 31.
[37] It is authored by Professor Louise Gullifer and available at https://stlrp.files.wordpress.com/2017/01/gullifer-registration.pdf.
[38] In contrast the Register of Statutory Pledges should be viewed strictly as a register of rights as it requires to take account of the fact that a statutory pledge once created can be amended, transferred or extinguished. See para 29.12 below.
[39] On RoA Rules, see Chapter 11 below.

27. The assignation document should be registered.

(Draft Bill, s 21(1)(h))

Form and protection of the RoA

6.31 The modern international standard for registers of assignations and security rights over moveable property[40] is that these are held in electronic form. This of course is also true of the Land Register of Scotland.[41] We therefore consider that the Keeper should keep the RoA in electronic form. Nevertheless, in line with the position under the Land Registration etc. (Scotland) Act 2012 and in the interests of flexibility,[42] we do not formally recommend that this should be required by statute.[43] Subject to the new statutory rules which we recommend, the exact detail should be a matter for the Keeper. But we would expect her to consult with key stakeholders in the finance and legal sectors. As with the Land Register,[44] we consider that the Keeper should be under a duty to take such steps as appear reasonable to her to protect the RoA from interference, unauthorised access or damage.

6.32 We recommend:

28. (a) Subject to the requirements of statute, the register should be in such form as the Keeper thinks fit.

(b) The Keeper should take such steps as appear reasonable to her for protecting the register from interference, unauthorised access, or damage.

(Draft Bill, s 19(3) and (4))

Applications for registration: paper or online or both?

6.33 In the Discussion Paper, we considered whether applications should be in paper form or online, or both.[45] We noted that online is simpler, quicker and cheaper. It is also more environmentally friendly. Nevertheless, we said that online applications would require fairly high-level digital signatures, and few debtors, and not all creditors, would have such signatures. We therefore thought that both paper and digital applications should be possible.

6.34 We have subsequently rethought our position because of the changes to the company charges registration regime which came into force on 1 April 2013 and also the position in comparator registers abroad. Electronic filing is now possible in the Companies Register. As discussed above, a certified copy of the charge instrument must be registered, but an instrument which has been signed and certified in ink can simply be scanned and transmitted electronically to Companies House. We see no reason why the same should not be possible in the RoA. This would help keep costs down.

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[40] Generally, known as Personal Property Security Registers.
[41] See Reid and Gretton, *Land Registration* para 3.7.
[42] For example, if there was a major IT malfunction and the Keeper had to resort to using paper for a short time.
[43] LR(S)A 2012 s 1(4).
[44] LR(S)A 2012 s 1(5). See Reid and Gretton, *Land Registration* para 3.8.
[45] Discussion Paper, paras 20.39–20.41.

6.35 The UK Government has noted that transactions completed using digital channels generally cost much less – for example the cost to Government per driving test booked in 2013 was £6.62 when post was used, £4.11 when telephone was used and just £0.22 when an online booking was made.[46] Companies House differentiates between the cost of paper registration and electronic registration of charges: with effect from 6 April 2016 it costs £23 for the former but only £15 for the latter.[47] There is also a high rate of use of digital services: most services which the UK Government offers as a digital service have a take-up rate of over 90%.[48]

6.36 Electronic-only registration is becoming the standard position internationally.[49] The New Zealand Personal Property Securities Register (PPSR) has only permitted electronic registrations since it was first established in 2002. This apparently was a deliberate policy decision to compel users to use remote access and to minimise the Registrar's responsibilities.[50] The new Belgian register is also to work on an electronic-only basis. When the Australian PPSR was set up in 2012 there was a facility for manual registrations. This facility was barely used. In the first year of operation only 21 of the 1,446,308 registrations were made manually.[51] The Registrar discontinued the service in July 2013.

6.37 At the moment there is almost no electronic-only registration for property or company transactions in Scotland.[52] But it is telling that when advance notices were introduced under the Land Registration etc. (Scotland) Act 2012, with effect from 8 December 2014, the figures from that date until 21 June 2015 were 55,126 electronic registrations and one paper registration.[53] The paper registration was not made by a solicitor. In addition Registers of Scotland have now consulted on making electronic-only registration possible for certain deeds in the Land Register, namely dispositions, standard securities and discharges.[54] Secondary legislation to provide for this is expected in 2018.[55]

6.38 The registration of assignations and statutory pledges in the RoA would normally be carried out by solicitors and businesses (especially financial institutions). In 2014 96% of businesses in the UK with ten employees or more had fixed broadband access and 81% had a website.[56] In 2016 the internet was used daily or almost daily by 82% of adults in Great

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[46] See https://gds.blog.gov.uk/2013/01/17/gov-transaction-costs-behind-data/.
[47] See https://www.nibusinessinfo.co.uk/content/companies-house-fee-changes-april.
[48] See https://www.gov.uk/performance/services.
[49] More broadly, advances in information technology have helped facilitate reform. See L Gullifer, "Conclusions and Recommendations" in Gullifer and Akseli (ed), *Secured Transactions Law Reform* 505 at 510.
[50] See Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 455–456.
[51] Australian Statutory Review 2015, para 6.11.1.
[52] Not all Companies House registration functions can be carried out online. See https://www.gov.uk/government/organisations/companies-house/about/about-our-services.
[53] We are grateful to Registers of Scotland for this information.
[54] See Registers of Scotland, *Digital Transformation: Next Steps* (November 2016) available at http://www.gov.scot/Resource/0051/00510886.pdf.
[55] See https://www.ros.gov.uk/about-us/news/2017/new-year-to-signal-next-steps-in-digital-transformation.
[56] See http://www.ons.gov.uk/businessindustryandtrade/itandinternetindustry/bulletins/ecommerceandictactivity/2014

Britain and 77% of adults bought goods or services online,[57] but use of the internet was generally lower by those with a disability.[58]

6.39 We think it unlikely that individuals without internet access or who are unable to use the internet would want to register assignations themselves. Allowing the option of paper registration would in our view increase costs without sufficient countervailing benefit. Ultimately the matter should be for the Scottish Ministers and Registers of Scotland, but we recommend:

29. Registration should be by electronic means only.

Automated registration with no checking by the Keeper

6.40 The Discussion Paper did not expressly address the issue of the extent to which the Keeper should check applications for registration. Clearly, there would have to be compliance with certain requirements such as using the correct form of application and paying the requisite fee. We consider these further in the next chapter. But should the Keeper check the application for mistakes? For example, in the application for registration it might be stated that the relevant assignation is by John in favour of the Bonnyrigg Bank, but the accompanying copy assignation document narrates an assignation by Kirsty in favour of the Bonnyrigg Bank. The Keeper, if required to check what is to enter the register, should notice the mistake and "bounce" the application.

6.41 This is the system in the Land Register[59] where an incoming application for registration is considered by the Keeper and, if satisfied, she gives effect to it.[60] A similar system operates at Companies House. Applications are considered and if the registrar is not content then the application will be refused. Such a system has several consequences. First, employing and training staff to check applications costs money. Second, it takes time. Thirdly, where the staff are responsible for transferring data from the application onto the register, there is the possibility that errors are made. In *Sebry v Companies House*[61] a notice that a company was in liquidation was erroneously registered by a member of staff at Companies House against the wrong company. Suppliers and creditors of that company, including its bank, became aware of the notice and refused to give the company credit, resulting in it going into administration. The result of the error in short "was a disaster for the company."[62] Companies House was held to have a duty of care to that company, which it breached by reason of the error.[63]

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[57] See http://www.ons.gov.uk/peoplepopulationandcommunity/householdcharacteristics/homeinternetandsocialmediausage/bulletins/internetaccesshouseholdsandindividuals/2016.

[58] See http://www.ons.gov.uk/peoplepopulationandcommunity/householdcharacteristics/homeinternetandsocialmediausage/datasets/internetaccesshouseholdsandindividualsreferencetables (Table 8).

[59] Other than for automated registration of title to land (ARTL), on which see Reid and Gretton, *Land Registration* ch 19.

[60] See generally LR(S)A 2012 Part 2 and Reid and Gretton, *Land Registration* para 8.10.

[61] [2015] EWHC 115 (QB), [2016] 1 WLR 2499.

[62] [2015] EWHC 115 (QB), [2016] 1 WLR 2499 at para [37] per Edis J.

[63] Since 1 April 2013 the role of the registar has become more limited as there is no checking of the particulars submitted against the charge document. See L Gullifer and M Raczynska, "The English Law of Personal Property Security: Under-reformed?" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 271 at 277.

6.42 The UCC–9/PPSA approach is different. All that is registered is the financing statement and the registrar does not verify the details. Modern information technology means that registration can work on an automated electronic basis. The UNCITRAL Guide on the Implementation of a Security Rights Registry of 2014 identifies six advantages of this approach.[64] First, it is cheaper, because of the lack of staff involvement. Registers of Scotland advise us that the cost to process an electronic application under an automated system is approximately five times cheaper than processing a paper application. Secondly, it is quicker. The application is dealt with almost instantaneously on receipt by the computer system. Thirdly, the register can be open 24/7, 365 days a year subject to closure for maintenance work. Fourthly, there is no room for human error on the part of the staff at the register. It is the computer system which processes the application system and transfers the submitted data onto the register. Fifthly, the possibility for fraudulent or corrupt conduct on the part of the staff at the register is reduced. Sixthly, there is a reduction in the potential liability of the register to users who might suffer a loss due to errors or dishonest conduct by its staff.

6.43 Cumulatively, these arguments are compelling. As Professor Louise Gullifer has noted: "in most electronic systems the role of the registrar is entirely administrative."[65] This is the model which the Secured Transactions Law Reform Project favours for England and Wales.[66] We have discussed this approach both with our advisory group and with Registers of Scotland. They were supportive of it. It was agreed that the responsibility for making sure that the information in an application for registration is correct should lie on the party making it and, where applicable, their agents such as solicitors who make the application on their behalf.

6.44 An automated system can be designed in a way which reduces the potential for errors. There are a number of possibilities. First, the registrant could be required to register itself on the system before any registration can be made. This registration could be used to pre-populate the online form. A postcode gazetteer could be used to provide and standardise addresses. The system could be set up not to accept a registration where any of the required data fields (such as the assignor's name and address) are not completed. There could be a link to the Companies House website to check a company's registered number. Double keying (requiring the same information to be entered twice) could be used to check for typographical errors. The ability to edit the application at any time while it is being completed and also at the end before final submission should also help. We understand from Registers of Scotland that the use of a "smart/intuitive" application form has decreased errors in land registration applications.

6.45 We recommend:

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[64] UNCITRAL Guide on the Implementation of a Security Rights Registry paras 83 to 85.

[65] L Gullifer, "Conclusions and Recommendations" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 505 at 523.

[66] See its Policy Paper of April 2016, available at https://securedtransactionslawreformproject.org/draft-policy-paper/ and its Discussion Paper on Registration (authored by Professor Louise Gullifer) of January 2017, available at https://stlrp.files.wordpress.com/2017/01/gullifer-registration.pdf.

30. Registration should be by means of an automated system under which applications are not checked by the Keeper.

(Draft Bill, s 119)

Chapter 7 Register of Assignations: structure, content and applications for registration

Introduction

7.1 In this chapter we consider the structure of the RoA, the data and documents that should be contained within it and the application process for registration.

Structure of the RoA

7.2 The RoA would be a register of assignations of claims. But in line with the position in the Land Register,[1] we consider that there should also be an archive record, in which archived material is kept by the Keeper. The circumstances in which an entry for assignation would be archived would be rare and be limited to where the register was corrected, for example where the registration was found to have been made frivolously or vexatiously.[2] In the Discussion Paper we asked consultees whether they agreed that superseded data should be archived.[3] Most consultees who responded to this question agreed, including the Keeper. We discuss archiving in more detail later,[4] but at this stage we recommend:

> **31. The Keeper should make up and maintain, as parts of the Register of Assignations:**
>
> **(a) the assignations record and**
>
> **(b) the archive record.**
>
> (Draft Bill, s 20)

Assignations record

7.3 In the previous chapter we recommended that assignation documents should be registered.[5] But a register comprising merely documents would not be user-friendly. Nor would it be easy to search. At the very least it would be essential that there was some form of indexing. A far preferable approach is to have an entry for each assignation document. The entry would contain key information such as the names of the parties and the date and time of registration. This would allow direct searching against certain data fields just as under the UCC–9 and PPSA systems. We deal with the subject of which fields should be

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[1] LR(S)A 2012 s 14. See Reid and Gretton, *Land Registration* para 4.31.
[2] On corrections see Chapter 9 below.
[3] Discussion Paper, para 20.54.
[4] See paras 11.19–11.21 below.
[5] See paras 6.13–6.30 above.

directly searchable in Chapter 10. Our draft Bill makes provision for the information that is to be contained in the records and includes power for the Scottish Ministers to make rules (known as RoA Rules)[6] setting out more detailed requirements.

7.4 In relation to what data should be required in the entry (and thus in the application for registration), inspiration can be drawn from UCC–9 and the PPSAs, although of course they make provisions for registers of security interests.[7] The fundamental point is that the RoA would be a person-based register, rather than a property-based register and the identification of the parties is crucial. We are of the view that the following data should have to appear.

(1) *Assignor's name and address*

7.5 The entry should reveal the assignor's name and address. To facilitate searching, the RoA Rules would specify what the assignor's "proper name" should be, that is to say the name that must be used in the register.

7.6 For individuals, the proper name could be that as shown on the person's driving licence or passport or birth certificate. An advantage of using the birth certificate name is that it is unusual for birth certificates to change.[8] The names on passports and driving licences more commonly change, notably on marriage. But passports and driving licences are documents which are generally more readily at hand. There is also something counter-intuitive about the idea that a woman who has been married and used her husband's name for 50 years should be identified by her maiden name.[9] In any event, there would need to be a hierarchy of identification documents prescribed by the rules, for example, current driving licence, which failing current passport, which failing birth certificate. Otherwise, there would be confusion.[10] For sole traders, we think that the individual's name rather than the trading name should be used, because this may be less likely to change and, moreover, is to be objectively determined from the documentation specified by the rules.[11]

(2) *Assignor's date of birth*

7.7 We think that where the assignor is an individual, the assignor's date of birth should require to be in the entry. The reason is that the assignor's name is unlikely to be unique.[12] For example, Registers of Scotland have advised us that a sample search against "Andrew Brown" which they conducted in the Land Register across all counties produced 112 results. If the search criteria are changed to "Andrew + [middle name] + Brown" there are 206 results. While not possible in the Land Register, a combined name and date of birth search

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[6] See paras 11.43–11.49 below.
[7] But some assignations require to be registered. See para 5.5 above.
[8] But it is possible for it to be changed under the Gender Recognition Act 2004.
[9] Under the Canadian PPSAs, the name as per the birth certificate is the standard identifier for individuals with a birth registered in that country, but if a name is changed following marriage it is that latter change that should be used. See Cuming, Walsh and Wood, *Personal Property Security Law* 341–344.
[10] See Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 478–481.
[11] Notwithstanding the fact that under rule 5.7 of the Ordinary Cause Rules most small businesses are identified in sheriff court actions by their trading name.
[12] With some exceptions.

would clearly generate far fewer results. Thus date of birth is registered, for example, under the Ontario, New Zealand and Australian PPSAs and under the Jersey legislation.[13]

7.8 The further advantages of using date of birth are that it is fixed and verifiable: an individual's date of birth can be found on that person's passport, driving licence, birth certificate, and marriage or civil partnership certificate. It is also used in many other contexts such as credit and proof of age checks, as well as taxation. There are of course disadvantages. The appearance of someone's date of birth on a public register can be regarded as an invasion of that person's privacy. And the availability of such information could assist identity theft. In our Report on Land Registration we recommended that the designation of individuals in the Land Register should include their date of birth to facilitate more accurate identification.[14] This recommendation was not taken forward into the Land Registration etc. (Scotland) Act 2012 and we understand that concerns about fraud influenced this.

7.9 We think that the case for using dates of birth is stronger in the RoA than in the Land Register because the former is a person-based register. There are, however, ways to reduce the concerns about privacy and fraud. With effect from October 2015, the Companies Register only shows the month and year of a company director's birth and not the day (although the full date of birth is submitted to Companies House).[15] A similar approach could be taken in the RoA. But we think that even more could be done. The individual's date of birth would be registered but not shown at all on the face of the register. But a search against that person's name and date of birth would take the searcher to the entry if there were one. We understand that date of birth has to be provided to register a croft in the Crofting Register established under the Crofting Reform (Scotland) Act 2010 but is not shown on the register.[16]

(3) *Assignors: unique number and other information*

7.10 Some legal persons have unique identifying numbers. Examples include UK companies and LLPs. These numbers do not change and there are clear advantages therefore in using them as a means of identification in order to facilitate searching. It is a requirement in the Land Register that a company is designed by reference to its registered number.[17] We would expect that the RoA Rules would require the unique number of companies, LLPs and some other legal persons to appear on the register. While charities have a registered number, not all charities have legal personality[18] and ones which do are typically structured as companies limited by guarantee and have a company number. Therefore charity numbers do not appear suitable for designation for these purposes. It is

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[13] See s 3(1)(c) of the Minister's Order under the Ontario PPSA 1990 available at https://www.ontario.ca/page/ministers-order-personal-property-security-act-1990; the NZ PPSA 1999 s 142(b); the Australian PPSA 2009 s 153 and the Security Interests (Registration and Miscellaneous Provisions) (Jersey) Order 2013 art 8(2)(e).

[14] Scottish Law Commission, Report on Land Registration (Scot Law Com No 222, 2010) paras 4.18–4.24.

[15] See https://companieshouse.blog.gov.uk/2015/06/17/great-news-were-listening-to-our-customers-and-making-changes/.

[16] Admittedly it is not used for searching purposes either, but the RoA could be different.

[17] LR(S)A 2012 s 113(1). See also NZ PPSA 1999 s 142(c).

[18] For example, they may be trusts.

perhaps unlikely that foreign entities would be required by RoA Rules to give their number because this would lead to complexity.[19]

7.11 There are also unique numbers used for individuals, such as VAT (value added tax) registration numbers, NI (national insurance) numbers and CHI (community health index) numbers, but whether any of these could be used may be more open to question.[20]

7.12 It may be helpful in some instances for other information relating to the assignor to be prescribed by RoA Rules. For example, where a partnership is the assignor it could be helpful to require the names and addresses of the partners to be registered too. Where the assignor is a trustee, it may be helpful to require that fact to be stated, along with the name of the trust.

(4) *Assignee's name and address*

7.13 Clearly, the assignee's name and address should also be given. The RoA Rules would set out more precisely what is required, but as we consider that the RoA should not be directly searchable against the assignee,[21] the requirements could be less rigorous.

(5) *Assignees: unique number and other information*

7.14 As recommended in relation to assignors, the RoA Rules should be able to specify when a unique number of an assignee is to be registered as well as any other required information. We think that the entry should also include an address to which requests for information regarding the assignation can be directed, such as enquiries about precisely which claims are assigned.[22] This might be an e-mail address. For example, in a large bank it would be helpful to have the details of the relevant department rather than just that of the head office.[23]

(6) *Identification of assigned claim*

7.15 While the assignation document would be registered and it would identify the claim or claims being assigned,[24] there may be benefit in providing that a form of identification should also be required or permitted as part of the data in the entry. While this would be a matter for RoA Rules, it may be helpful to explore options here.

7.16 For example, there might be tick boxes to be completed when an application for registration is being made with categories such as "rents", "royalties" and "invoices for goods or services". A third party interested in the rents who saw that the box for rents had not been completed would be saved the need to look at the assignation document. Such a system is used in the Ontario, New Zealand and Australian PPSAs.[25] But in New Zealand for all property types other than "all present and after-acquired property" a verbal description is

[19] Given the huge number of possible entities and jurisdictions.
[20] Only individuals who are sole traders and are registered for VAT have VAT numbers and we understand that such numbers can change. NI and CHI numbers raise privacy issues and not all individuals (such as those who have recently moved to the UK) have them.
[21] See below, para 10.3.
[22] See below, paras 11.2–11.14.
[23] Compare NZ PPSA 1999 s 142(d) and Australian PPSA 2009 s 153 item 3.
[24] For the extent to which the claims need be described in the assignation document see paras 4.21–4.25 above.
[25] See general the Australian Statutory Review 2015 paras 6.3.1–6.3.3.

also required. In Australia the statutory reviewer has recommended that the number of asset classes is reduced.[26]

7.17 If there is a tick box system, one concern might be that applicants for registration would simply tick all the boxes to avoid any chance that a class of claim was mistakenly omitted. The tick boxes would then be uninformative if this became general practice. But this objection can be met by having a correction procedure, under which the assignor could require removal of inaccurate ticks.[27]

7.18 In the Canadian PPSA jurisdictions apart from Ontario there is not a "tick box" system. Instead the property must be described in the same way as under the security agreement. This may be by reference to an "item" or "kind" and can therefore be a generic description such as "automobiles" which does not identify which particular cars are covered.[28] It is understood that the Ontario legislation is to be amended to follow this approach too.[29]

7.19 Of course under the UCC–9/PPSA approach there is no document registration. This contrasts with the position for registration of charges in the Companies Register since 1 April 2013. There the document is registered, but the relevant application form[30] contains the following box:

> "4. Brief description. Please give a short description of any land, ship, aircraft, or intellectual property registered or required to be registered in the UK subject to a charge (which is not a floating charge) or fixed security included in the instrument."

7.20 These asset classes all have specialist registers and the point of box 4 seems to be more to remind the party registering that registration in the specialist register is also required for the charge (security right) to have third party effect.

7.21 A further option would be to require the applicant for registration to reproduce the description of the claim in the assignation document. But such an approach would seem to undermine one of the main reasons for requiring that document to be registered and would run contrary to the reforms made to company charges registration with effect from 1 April 2013.

7.22 We would expect consultation on what (if any) type of description should be required before RoA Rules are made.

(7) *Copy of the assignation document*

7.23 As discussed earlier,[31] the entry would include a copy of the assignation document.

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[26] Australian Statutory Review 2015, para 6.3.3.
[27] See paras 9.10–9.22 below.
[28] See R C C Cuming and R J Wood, *Saskatchewan and Manitoba Personal Property Security Acts Handbook* (1994) 111.
[29] See Cuming, Walsh and Wood, *Personal Property Security Law* 349.
[30] Form MR01, available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/537724/MR01_v2.1.pdf
[31] See paras 6.13–6.30 above.

(8) *Unique registration number*

7.24 Each entry should have a unique registration number rather like a title number in land registration. This is standard under comparator legislation.[32]

(9) *Date and time of registration*

7.25 The date and time of registration are important for priority purposes and would be added to the entry by the Keeper's computer system.

(10) *Other data*

7.26 The entry should also contain any other data required under the new legislation or under RoA Rules made by the Scottish Ministers. For example, when a correction to data is made the details of that correction and the date and time it is made should require to appear.[33]

7.27 Drawing this together, we recommend:

32. An entry in the assignations record should include:

(a) the assignor's name and address,

(b) where the assignor is an individual, the assignor's date of birth,

(c) any number which the assignor bears or other information relating to the assignor which, by virtue of RoA Rules, must be included in the entry,

(d) the assignee's name and address,

(e) any number which the assignee bears or other information relating to the assignee which, by virtue of RoA Rules, must be included in the entry,

(f) where the assignee is not an individual, an address (which may be an e-mail address) to which requests for information regarding the assignation may be directed,

(g) such description of the claim as may be required or permitted by RoA Rules,

(h) a copy of the assignation document,

(i) the registration number allocated to the entry,

(j) the date and time of registration of the assignation document, and

[32] Eg NZ PPSA 1999 s 144; UNCITRAL Model Law on Secured Transactions Model Registry Provisions art 1(j).
[33] See Chapter 9 below.

(k) such other data as may be required by legislation.

(Draft Bill, s 21(1))

Applications for registration

7.28 An application for registration would be made online. It would be the assignee who would apply to register the assignation document, in line with the normal rule of property law that it is the transferee who completes title.[34] It would be possible for applications to be made by agents such as solicitors.

7.29 We think that the Keeper should require to accept the application provided that certain conditions are satisfied. The application would have to conform to the requirements imposed by RoA Rules and be accompanied by a copy of the assignation document. The rules would set out the form of application and the data fields that require to be completed. The application would need to provide the Keeper with the necessary data to make up an entry in the register. It would of course also be essential for the applicant to pay the relevant registration fee.

7.30 We recommend:

33. (a) An application for registration of an assignation document should be made by or on behalf of the assignee.

(b) The Keeper should be required to accept an application if:

(i) it conforms to RoA Rules in relation to applications,

(ii) it is submitted with a copy of the assignation document,

(iii) it provides the Keeper with the necessary data to make up an entry for the assignation in the RoA, and

(iv) the registration fee is paid or the Keeper is satisfied that it will be.

(c) Where these requirements are not satisfied, the Keeper should be required to reject the application and inform the applicant accordingly.

(Draft Bill, s 23(1) to (3) and 118(4))

Creation of an entry in the assignations record

7.31 An entry in the assignations record would be made up as follows. The Keeper (or more accurately the automated computer system under her management) would receive the application for registration of the assignation document. Assuming that it was in acceptable

[34] But compare the position as regards intimation. See paras 5.38–5.39 above.

terms,[35] an entry would be created and a unique number allocated to it. The entry would thus be made up by the Keeper's automated computer system from (i) the data provided in the application; (ii) the circumstances of registration, in particular the date and time; and (iii) the copy of the assignation document. We envisage that (i) and (ii) would be presented in a similar way to notice filing registers as under UCC–9 and the PPSAs. As regards (iii) it would be possible for anyone inspecting the entry to view this too.

7.32 We recommend:

> **34. On accepting an application for registration, the Keeper should be required to:**
>
> **(a) make up and maintain in the assignations record an entry for the assignation document, and**
>
> **(b) allocate a registration number to the entry.**
>
> (Draft Bill, s 23(4))

Verification statements

7.33 Under automated registration systems elsewhere such as in the UCC–9/PPSA jurisdictions a verification statement is sent to the applicant for registration confirming that the registration has been successful.[36] The statement normally contains the data that has been registered along with the date and time of registration and the unique number allocated to the entry. We think that there should be a similar system in the RoA. The form of the statement would be set out in the RoA Rules. We understand from Registers of Scotland that in relation to an application for registration in the Land Register the applicant can specify up to four e-mail addresses to which the receipt of the application is sent. The same could happen with the RoA.

7.34 Some PPSAs require the secured creditor to send a copy of the verification statement to the provider, although this can be contracted out of by the parties.[37] The purpose of this is to enable the person named as the debtor in the financing statement to be informed of the existence and content of the registration as it may affect the future ability of that person to obtain credit.[38] Under the DCFR Book IX, where the provider has to be accredited by the system, the verification statement is sent directly to that party.[39]

7.35 There is benefit to the assignee in sending a verification statement to the assignor. That person can ask the assignor to check that it is correct and thus obtain further assurance that the registration is effective.[40]

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[35] See para 7.29 above.
[36] See eg NZ PPSA 1999 s 145; Australian PPSA ss 155 and 156; DCFR IX.–3:313; UNCITRAL Model Law on Secured Transactions Model Registry Provisions art 15. See also Allan, *The Law of Secured Credit* 449–450.
[37] Eg NZ PPSA 1999 s 148; Australian PPSA 2009 s 157.
[38] Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 468.
[39] DCFR IX.–3:313.
[40] Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 468–469.

7.36 We think that the duty to provide a copy of the verification statement is important under the UCC–9/PPSA approach where the financing statement can be registered unilaterally by the secured creditor with no involvement from the party named as the debtor. In the RoA matters would be rather different. Registration would be of an assignation which the assignor has granted.[41] There is no requirement for the secured creditor to confirm the details of registration in the legislation on standard securities and floating charges.[42]

7.37 If a duty were to be imposed we anticipate that financial institutions would wish the right to contract out of this as is the position in Australia and New Zealand. There is also the issue of what sanction there should be for breach of that duty. The UNCITRAL Model Law on Secured Transactions suggests that a nominal amount should be payable to the grantor of the security right, as well as any compensation for any actual loss or damage.[43]

7.38 Another possibility is that the verification statement is sent directly by the Keeper's computer system to the assignor as well as the assignee. But unless an accreditation system along the lines contemplated by the DCFR were used, the statement would be sent to the e-mail address provided by the assignee. This could be wrong.

7.39 On balance our view is that there should not be an obligation on the assignee to send a copy of the statement to the assignor although, as we have noted, it may be in the assignee's interests to send it as the assignor may notice any errors. But we think that the assignor should have the right to request a copy of it from the assignee in order to check the details that have been registered. The assignee should have 21 days to comply.

7.40 We recommend:

35. (a) The Keeper should be required to issue a verification statement on accepting an application for registration.

(b) The statement should require to conform to RoA Rules. It should include the date and time of the registration and the registration number allocated to the entry to which the application relates.

(c) The assignor should be entitled to obtain a copy of the verification statement from the assignee and the assignee should be required to supply the copy within 21 days after the request is made.

(Draft Bill, s 24)

Date and time of registration

7.41 The date and time of a registration are crucial for priority purposes. The Keeper's computer system would determine when the relevant entry is made up and that date and time should be stated in the entry. Given that it is possible for a computer system to record the time of receipt with a high degree of accuracy, perhaps to the nearest second, it is highly unlikely that two registrations would be made at exactly the same time. But if that were the

[41] Of course there is the possibility of a forgery.
[42] Conveyancing and Feudal Reform (Scotland) Act 1970 Part 2; Companies Act 2006 Part 25.
[43] UNCITRAL Model Law on Secured Transactions, Model Registry Provisions art 15(4).

case, we think that the registration in respect of which the application reached the Keeper first should have priority.[44] The computer system should be able to determine which application that is.

7.42 We recommend:

> **36. (a) A registration should be taken to be made on the date and at the time which are entered for it in the Register of Assignations.**
>
> **(b) The Keeper should be required to deal with applications for registration and allocate these registration numbers in order of receipt.**
>
> (Draft Bill, s 25)

Retrocessions

7.43 Often assignations are one-off transactions. The claim is transferred to the assignee and that is that. But in other situations, notably assignations in security, there may well be a re-assignation or, to use the technical term, *retrocession*, if the debt secured is repaid. For example, a landlord might assign the rents due to it from a tenant in return for a loan from the bank. The bank then becomes entitled to the rents. In practice it will not uplift these unless there is default on the loan. But if the loan is repaid the landlord will seek a retrocession.

7.44 The question then arises as to how effect should be given to the retrocession in the Register of Assignations. The position under UCC–9 and the PPSAs is that the assignation is recharacterised as a security interest and the notice on the register giving it priority is simply cancelled on the loan being repaid. In Scotland, however, an assignation in security is a transfer and not a right or interest, and therefore cannot simply be cancelled.[45] As discussed elsewhere in this Report, our consultees opposed recharacterisation.[46]

7.45 We considered a system under which a retrocession could be registered against the same entry as the original assignation, but decided against this for reasons of complexity. It might be, for example, that only some of the claims are retrocessed.

7.46 We have reached the view that a retrocession should be treated like other assignation documents and result in its own entry. This reflects the current position in practice for assignations of rents where typically the parties choose to record the assignation and the eventual retrocession in the Books of Council and Session.

7.47 The Keeper, however, may wish to consider whether it would be possible to have a link between the entries. Thus in the application for registration the applicant might be asked to state whether the assignation is a retrocession and, if so, whether it relates to an

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[44] See the LR(S)A 2012 s 39(1).

[45] This was an issue which was encountered at an earlier stage in Scotland in relation to the *ex facie* absolute disposition, a form of heritable security prior to the introduction of the standard security, for which statute incoherently provided a form of discharge. See G L Gretton, "*Ex Facie* Absolution Dispositions and their Discharge" 1979 JLSS 462.

[46] See para 18.46 below.

assignation that has already been registered. If the registration number of that entry is then provided by the applicant the computer system could put a flag on the original entry.[47]

[47] Such an approach would address the concern of ICAS in its response to our draft Bill consultation of July 2017 that it would help business to discover simply that a financing arrangement is at an end.

Chapter 8 Register of Assignations: effective registration

Introduction

8.1 The purpose of the Register of Assignations is to alert third parties to the existence of an assignation of a claim. This clearly necessitates certain requirements for a registration to be effective to transfer the assigned claim. As noted earlier,[1] the RoA is to be a person-based register. It is therefore crucial that a registration against that person is made in a way that someone searching the RoA can discover it. Thus it would defeat the point of registration if it were acceptable for an assignation granted by Esmerelda to be registered against Suzanna as assignor rather than Esmerelda. Someone searching the RoA against Esmerelda would not find the assignation and would thus be misled.

8.2 This chapter considers the concept of effective registration in the assignations record. We note that the idea of effective registration is also found in the Australian PPSA 2009[2] and the UNCITRAL Model Law on Secured Transactions of 2016,[3] but there the effectiveness relates to registration of a notice (of a security interest). In contrast our concern is with the transfer of a claim by means of an effective registration of an assignation document.

Effective registration

8.3 We consider that it should be made clear where a registration would fail to be effective. In these circumstances the claim would not be transferred. Two categories can be identified: (1) failings in relation to the assignation document; and (2) failings in relation to the data in the entry.

(1) *Entry does not include a copy of the assignation document or document is invalid*

8.4 Earlier we recommended that (a copy of) the assignation document should be registered.[4] Thus if a PDF of a blank sheet of paper is uploaded instead, or a copy of the wrong assignation, or a materially flawed scan with missing text there would be no effective registration. Similarly, the registration would not be effective if it were of an invalid document such as a forgery.

(2) *Entry contains an inaccuracy which is seriously misleading*

8.5 A registration should also fail if the entry created in the assignations record contains a seriously misleading inaccuracy in relation to the registered data. This rule deals with the

[1] See para 7.4 above.
[2] Australian PPSA 2009 s 163. See too Allan, *The Law of Secured Credit* 451.
[3] UNCITRAL Model Law on Secured Transactions, Model Registry Provisions arts 23–25.
[4] See paras 6.13–6.29 above.

situation described above where Suzanna is named as the assignor in the entry for an assignation which was actually granted by Esmerelda.

8.6 In the Discussion Paper, we noted our understanding that in the UCC–9 and PPSA systems errors are common,[5] but that an inaccuracy only invalidates an entry if it would have misled a person searching the register with ordinary diligence. The test is thus an objective one. It does not depend on someone actually being misled. We described the test therefore as one of "reasonable findability". We referred to the relevant provision in the Ontario PPSA: "A financing statement or financing change statement is not invalidated nor is its effect impaired by reason only of an error or omission therein or in its execution or registration unless a reasonable person is likely to be misled materially by the error or omission."[6]

8.7 We wondered, however, whether there was a case for a tougher approach, namely that any mistake would invalidate the registration, in the same way as a key that is *almost* correctly cut will not open the lock. Unlike under the functional approach of UCC–9 and the PPSAs almost all the parties registering would be banks and other financial institutions, or lawyers acting on their behalf. Such a tough approach could be argued for in utilitarian terms, on the basis that the occasional unfairness to particular persons would be justified by benefits to the system as a whole, by incentivising application forms to be completed accurately.

8.8 We therefore asked consultees whether errors should be subject to a "reasonable findability" test. In other words, errors that did not prejudice "reasonable findability" would not matter, but errors which did prejudice "reasonable findability" would be fatal to the validity of the entry, whether or not anyone had in fact been misled. We asked alternatively whether the validity of an entry should depend on its being error-free.

8.9 The consultees who directly answered these questions tended to support a "reasonable findability" test rather than the entry being required to be error-free. For example, Dr Ross Anderson said that the law "should be slow to invalidate the reasonable expectations of business people on the basis of immaterial technicalities." Several law firm consultees, while supporting this approach, noted that there would probably require to be litigation to determine the parameters of what "reasonable findability" meant.

8.10 On reflection, we agree that error-free is too severe a standard to require and that minor errors which do not mislead a searcher should not render a registration ineffective. In the Discussion Paper, as noted above, we referred to the Ontario PPSA where the test is that the searcher is "misled materially". In fact the more common wording used in legislation internationally is that the registration fails where there is an error or omission in the entry which is "seriously misleading". We refer to UCC–9,[7] the Australian PPSA 2009,[8] the New Zealand PPSA 1999,[9] the Canadian PPSAs other than Ontario,[10] the Vanuatu PPSA 2010,[11]

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[5] Discussion Paper, para 20.36 under reference to J Ziegel, "A Canadian Academic's Reactions to the Law Commission's Proposals" in De Lacy (ed), *The Reform of UK Personal Property Security Law* 117 at 125.
[6] Ontario PPSA 1990 s 46(4).
[7] UCC § 9–506.
[8] Australian PPSA 2009 s 164.
[9] NZ PPSA 1999 s 149.
[10] Alberta PPSA 2000 s 43(6); British Columbia PPSA 1996 s 43(6); Manitoba PPSA 1993 s 43(6); New Brunswick PPSA 1993 s 43(6); Newfoundland and Labrador PPSA 1998 s 44(7); Northwest Territories and

the Tonga PPSA 2010,[12] the Papua New Guinea PPSA 2011,[13] the Security Interests (Jersey) Law 2012,[14] the Malawi PPSA 2013,[15] the Samoa PPSA 2013,[16] and the UNCITRAL Model Law on Secured Transactions of 2016.[17] It has been argued that there is no substantive difference between "seriously misleading" and the Ontario formulation of a searcher being "misled materially".[18]

8.11 In the light of its widespread use internationally we recommend the use of the "seriously misleading" test. We think that it more precisely describes the type of mistakes which should invalidate an entry than a "reasonable findability" test. On one interpretation, a "reasonable findability" test is satisfied if the relevant entry can be found. But, even once an entry can be found, it could contain an error which should invalidate the registration. Imagine that where an assignation is registered it is a requirement that the category of claim assigned is identified by means of a tick box system. The advantage of this is that it saves the searcher having to look at the assignation document if the searcher has no interest in the boxes that have been ticked. For example, Eugene might assign the royalties from his patent to Freddie. If Freddie registers the assignation and ticks a box for assignation of rents rather than royalties that error should render the registration ineffective.

8.12 We think that what requires to be "seriously misleading" is an inaccuracy in the entry. The terms "errors" and "omissions" can be found in UCC–9.[19] Other comparator legislation also mentions "defects" and "irregularities".[20] The term "inaccuracy", now familiar from the legislation on land registration,[21] seems to us to capture succinctly all these ideas.

8.13 The "seriously misleading" test would be applied at the time of registration in relation to the data registered. It is at that point that the details should be accurate. For example, in 2020 Anna Smith assigns to the Bearsden Bank the right to be paid the sum of £50,000 in 2022 which has been promised by her uncle. The assignation is registered in the RoA with Anna's correct details. The registration is effective. Anna marries in 2021 and changes her name to Anna Philip. This does not render the registration ineffective because the details are now inaccurate.

8.14 In relation to statutory pledges we recommend a good faith protection rule which would apply in such circumstances.[22] For an assignation, because of its different juridical nature as a transfer rather than a right, such a rule would be awkward. It would mean that the Bearsden Bank would have to update the register to protect itself against the relatively unlikely event of a second fraudulent assignation of the same claim by Anna to another party

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Nunavut PPSA 1998 s 46(4); Nova Scotia PPSA 1995 s 44(7); Prince Edward Island PPSA 1997 s 43(6); Saskatchewan PPSA 1993 s 43(6); Yukon PPSA 2002 s 64(1).

[11] Vanuatu PPSA 2010 s 126.

[12] Tonga PPSA 2010 s 47.

[13] Papua New Guinea PPSA 2011 s 82.

[14] Security Interests (Jersey) Law 2012 art 66(1).

[15] Malawi PPSA 2013 s 64.

[16] Samoa PPSA 2013 s 37.

[17] UNCITRAL Model Law on Secured Transactions Model Registry Provisions art 2. But the Belgian Pledge Act of 11 July 2013 art 20 (inserting a new art 15 into title XVII of book III of the Civil Code) uses the term "incorrectly identified" (*onjuiste identificatie/identification erronée*).

[18] Cuming, Walsh and Wood, *Personal Property Security Law* 363.

[19] UCC § 9–506.

[20] Eg Security Interests (Jersey) Law 2012 art 66.

[21] LR(S)A 2012 s 65.

[22] As to how a change of name should impact on a statutory pledge, see Chapter 32 below.

who was in good faith. Imagine, however, that the Bearsden Bank did not update the register and itself assigned the claim to another financial institution. That institution would lose out if there were a rule protecting a good faith party who had taken a second assignation of the same claim made by Anna.[23] Given that the RoA is not to be a definitive record of all assignations of claims (because the intimation option would remain available[24] as well as assignation without registration under the Financial Collateral Arrangements (No. 2) Regulations 2003[25]), due diligence with potential assignors would mean that enquiries beyond checking the register should take place and ascertaining any recent change of name could be part of that process.

8.15 Below, we consider the "seriously misleading" test in more detail, but before that we recommend:

> **37. The registration of an assignation document should be ineffective if:**
>
> **(a) the entry made up for it does not include a copy of the assignation document,**
>
> **(b) that document is invalid, or**
>
> **(c) there is an inaccuracy in relation to the data registered, which as at the time of registration, is seriously misleading.**
>
> (Draft Bill, s 26(1))

Seriously misleading inaccuracies in entries in the assignations record

Introduction

8.16 We noted above the concerns of some consultees that litigation would be required to test the parameters of which inaccuracies are allowable and which are not. We think that these concerns can be addressed at least to some extent by our draft Bill making more precise provision about when an inaccuracy is "seriously misleading". Another possible source of help is case law from other jurisdictions which use such a test, but caution must be exercised here as account has to be taken of the wording of the comparator legislation as a whole, together with the operation of the register in the particular jurisdiction in question.[26] In fact, we understand there has been relatively little case law on the test, which suggests that it generally works satisfactorily.

(1) *An objective test*

8.17 Further to the discussion above, it should be made clear that the "seriously misleading" test is an objective one. There should be no requirement to show that someone has actually been misled. An Ontario court has expressed the rationale as follows:

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[23] Unless the rule did not apply against subsequent assignees, but this would mean a more complicated rule.
[24] Except in any prescribed cases. See para 5.20–5.21 above.
[25] See Chapter 14 below.
[26] Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 471–472. See also Allan, *The Law of Secured Credit* 460.

> "The purpose for which the reasonable person uses the search function provides the key to determining when it can be said that the reasonable person would be materially misled by an error in a financing statement. The reasonable person uses the system to find prior registered secured interests in the property in question. If the error in the financing statement results in the reasonable person not retrieving that financing statement from the system, then the reasonable person will probably be misled materially. If despite the error, the reasonable person . . . will still retrieve the flawed financing statements from the system, then the error in the financing statement is not likely to mislead materially."[27]

8.18 An objective approach is the standard position internationally[28] and makes the application of the test simpler. There is a subtlety, however, between the approach in Ontario and that in the other Canadian PPSA provinces, New Zealand and Australia. The Ontario PPSA as mentioned above refers expressly to the concept of the "reasonable searcher". This appears to add an extra level of complexity. It is simpler to take the approach whereby an inaccuracy is seriously misleading if it prevents a registration being disclosed by a properly formatted search in the relevant searchable field.[29] We develop this approach further below.[30]

(2) *No account should be taken of assignation document*

8.19 We consider that in determining whether an inaccuracy is seriously misleading no account should be taken of the assignation document. Example 1. The entry for an assignation by Calum in favour of Joshua, mistakenly identifies the assignor as Anna rather than Calum. The fact that the assignation document gives the correct position, namely that Calum is the assignor, would not help the entry to be found as the search would be against the name of the assignor as stated in the data in the entry. Example 2.[31] The application form for registration in the assignations record has a tick box for classes of claim. Eugene assigns the royalties from his patent to Freddie. Freddie registers the assignation in the RoA and erroneously ticks a box for assignation of "rents" rather than "royalties". A searcher who is only interested in royalties is misled. The searcher should not be required also to look at the assignation document to see if there is a discrepancy. We note that under the Australian PPSA, where it is competent to register the security agreement, the "seriously misleading" test is limited to data in the entry.[32]

(3) *Registration ineffective in part*

8.20 We think that there should be express rules on inaccuracies which only render the registration ineffective in part. Such rules are typically found in comparator legislation.[33] Example 1. Alexander assigns to a bank (a) rents and (b) royalties due to him. The bank registers the assignation in the RoA but only ticks the box in the application form for rents and not the one for royalties. The registration is ineffective as regards the royalties.

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[27] *Re Lambert* (1994) 7 PPSAC (2d) 240 at para 46 per Doherty JA. See also *Gold Key Pontiac Buick (1984) Ltd v 464750 BC Ltd (Trustee of)* 2000 BCCA 435 at para 10 per Newbury JA.
[28] See eg NZ PPSA 1999 s 151; Australian PPSA 2009 s 164(2); Security Interests (Jersey) Law 2012 s 66(3).
[29] See *Polymers International Ltd v Toon* [2013] NZHC 1897 at para 23 per Asher J.
[30] See paras 8.21–8.28 below.
[31] See also para 8.11 above.
[32] Australian PPSA 2009 s 164(1)(a).
[33] See eg NZ PPSA 1999 s 152; Security Interests (Jersey) Law 2012 s 66(4); UNCITRAL Model Law on Secured Transactions, Model Registry Provisions art 24(3) and (5).

Example 2. Frances and Henry are the landlords of a shop. They assign the rents to James. He registers the assignation in the RoA, but when completing the application for registration states that Henry is the assignor but fails to mention Frances. The registration is only effective as regards Henry's share of the right to the rents. Example 3. Mairi assigns her right to copyright royalties to Belinda and Charles. Belinda (with Charles's consent) registers the assignation in the RoA, but when completing the application form for registration by mistake only states that Charles is the assignee. The registration is only effective as regards the share of the royalties assigned to Charles.

(4) *Specific cases where search does not retrieve entry*

8.21 We consider that circumstances in which it is clear that there would be a seriously misleading inaccuracy should be spelt out. Again, examples of this can be found in comparator legislation. For example, the Security Interests (Jersey) Law 2012 provides that, without limiting the operation of the test in general, a registration is invalid if there is a seriously misleading defect, irregularity, omission, or error, in any name, or registration number, required by secondary legislation.[34] A registration number would be the unique number of a corporate body, such as a company. The NZ PPSA 1999, again without restricting the operation of the test in general, provides that a registration is invalid if there is a seriously misleading defect, irregularity, omission, or error in the name of a debtor, or in the serial number of encumbered property where that serial number requires to be registered.[35] UCC–9 provides that a financing statement which fails sufficiently to provide the debtor's name is seriously misleading, but this will not be the case if a search "under the debtor's correct name using the filing office's standard search logic" discloses the statement.[36]

8.22 We have drawn on these models to formulate three rules whereby a search against the assignor's details at the date and time at which the entry is made up and which does not reveal the entry means that there is a seriously misleading inaccuracy.

8.23 The first would apply where the assignor (or co-assignor) is a person required by RoA Rules to be identified in the entry by a unique number. We have in mind companies and LLPs, which have unique registration numbers. These, unlike the body's name, do not change. If a search against that number did not retrieve the entry the registration should be ineffective because of this seriously misleading inaccuracy. In contrast an error in the name would not matter provided that the number was correct. But where the number was wrong although the name was correct this would not rescue the entry as getting the number correct would be regarded as essential.

8.24 The second rule would apply where the assignor (or co-assignor) is not required by rules to be identified in the entry by a unique number. We expect this rule to apply to individuals[37] and partnerships. If a search against the assignor's "proper name" does not retrieve the entry the registration should be ineffective. Reference can be made to the

[34] Security Interests (Jersey) Law 2012 art 66(2).
[35] NZ PPSA 1999 s 150.
[36] UCC § 9–506(b) and (c).
[37] It is not impossible that individuals might require to be identified by something like their National Insurance number, but we think that this is unlikely given concerns about privacy and fraud.

Canadian case of *KJM Leasing Ltd v Granstrand Brothers Inc*[38] where there was a registration against "Grandstrand Brothers Inc" rather than "Granstrand Brothers Inc" which was found to be seriously misleading and the court stated:

> "What a search under the incorrect name discloses is not the right question. Obviously a search under the incorrect name will disclose the Applicant's security. But it defies logic to say that a search under the incorrect name discloses the disputed security so the error is not seriously misleading. That is a circular argument. What is relevant is what a search under the right name will disclose. What will a searcher with the right name discover?"[39]

8.25 The meaning of "proper name" would be set out in RoA Rules and would be by reference to specified documentation such as driving licence, passport or birth certificate.[40]

8.26 The third rule would apply to assignors (or co-assignors) who are individuals. If a search against the assignor's "proper name" and date of birth does not retrieve the entry the registration should be ineffective. The advantage of a name and date of birth search is that it reduces the number of search results.[41]

8.27 All three of these rules would have common features. First, the search would be for the assignor's details as at the date and time the registration was made. It is at that moment that the details have to be sufficiently accurate to enable the search to retrieve them. Secondly, the search would be by means of a specific type of search facility which the Keeper would provide. In Chapter 10 below we explain how searches in equivalent registers overseas can have varying logic. In particular a distinction is made between "exact match" where there is little scope for error and "close match" where there is greater scope. We think that this matter should be for further discussion when the RoA is being developed. But, for example, if the RoA is to be an "exact match" register, an entry in the assignations record would have a seriously misleading inaccuracy if the assignor's name as stated in the entry did not exactly match the assignor's "proper name" as per the RoA Rules.

8.28 It should be stressed, however, that an entry may contain a seriously misleading inaccuracy even although it can be retrieved by a search, for example, where the wrong details are given for the assignee. (We do not envisage direct searching against the assignee for the reasons discussed elsewhere.[42])

(5) *Power to specify further instances in which an inaccuracy is seriously misleading*

8.29 We think that it would be helpful for the Scottish Ministers to have a power to specify other circumstances in which an inaccuracy is seriously misleading. For example, if the assignors are trustees the RoA Rules might require that the "proper names" of the trustees include the name of the trust for which they act. It might then be provided that there will be a seriously misleading inaccuracy if a search against the trust name does not retrieve the entry.

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[38] (1994) 7 PPSAC (2d) 197.
[39] (1994) 7 PPSAC (2d) 197 at paras 13–14 per Master Funduk.
[40] See para 7.6 above.
[41] See paras 7.7–7.9 above.
[42] See para 10.3 below.

8.30 Drawing all this together, we recommend:

38. (a) An inaccuracy in an entry in the assignations record may be seriously misleading irrespective of whether any person has been misled.

(b) In determining whether an inaccuracy is seriously misleading no account should be taken of the assignation document included in the entry.

(c) An inaccuracy which is seriously misleading in respect of part of an entry, as regards the details of the claim, assignor or assignee, should not affect the rest of the entry.

(d) Without prejudice to the generality, an inaccuracy should be seriously misleading:

(i) where the assignor (or, as the case may be, a co-assignor) is not a person required by RoA Rules to be identified by a unique number, if a search using a designated facility provided by the Keeper for

(a) the assignor's (or co-assignor's) proper name as at the date and time the entry was created, or for

(b) the assignor's (or co-assignor's) proper name as at that date and time and the assignor's (or co-assignor's) date of birth

does not disclose the entry;

(ii) where the assignor (or, as the case may be, a co-assignor) is a person required by RoA Rules to be identified by a unique number, if a search using a designated facility provided by the Keeper for that number as at the date and time the entry was created does not disclose the entry, including where a search using such a facility for the assignor's (or co-assignor's) number does disclose the entry.

(e) The meaning of "proper name" should be set out in RoA Rules.

(f) The Scottish Ministers should have the power to specify further instances in which an inaccuracy is seriously misleading.

(Draft Bill, s 27)

Chapter 9 Register of Assignations: corrections

Introduction

9.1 In this chapter we consider the issue of inaccurate entries in the Register of Assignations. We recommend rules as to how the inaccuracy could be corrected, with or without court intervention. Where an entry is entirely bad it would be removed from the assignations record and transferred to the archive record. In less severe cases it would merely be data within an entry that would be corrected. We begin by considering examples of inaccuracies.

Possible inaccuracies

Error by party which made the registration

9.2 A mistake could be made by the person who registered the assignation. For example, an assignation by Karl in favour of Leslie might be mistakenly registered against Kevin rather than Karl. This would be caused by the application for registration being completed incorrectly because it would be this application which would generate the entry by means of the automated computer system.[1] Other mistakes could be made in the application too such as identifying the category of claims wrongly (assuming such identification were required), say by ticking the box for "rents" rather than "royalties" where the assignation was of patent royalties. Another possibility would be the wrong copy document being uploaded instead of the copy of the relevant assignation. We envisage, however, that the automated computer system would require a copy document to be registered or the application would not be processed so that it would not be possible for an entry to be created with no document.

Frivolous or vexatious registrations

9.3 Since registration would be automated and the Keeper would not check applications, there would be a risk of frivolous or vexatious registrations being made. An example of a "frivolous" registration would be someone registering an assignation by Mickey Mouse in favour of Donald Duck. Hopefully, the registration fee would deter such practices, but nonetheless there should be a mechanism for the Keeper to delete nonsense entries. An example of a "vexatious" registration would be someone registering a false entry against a famous politician, which could potentially affect that person's credit rating. There have been some examples of this in the USA under UCC–9, although the experience from other jurisdictions generally is that the problem is not a significant one.[2]

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[1] See paras 6.40–6.45 above.

[2] See generally Drobnig and Böger, *Proprietary Security in Movable Assets* 490. But see the two Australian cases of *Sandhurst Golf Estates Pty Ltd v Coppersmith Pty Ltd* [2014] VSC 217 and *Macquarie Leasing Pty Ltd v DEQMO Pty Ltd* [2014] NSWC 1466.

9.4 Under the Land Registration (Scotland) Act 1979 (now repealed) the Keeper was bound to reject frivolous or vexatious applications for registration.[3] The Land Registration etc. (Scotland) Act 2012 takes an alternative approach: namely that invalid deeds should not be accepted.[4] But this is of course dependent on the Keeper looking at the application before giving effect to it. In contrast under the automated systems of UCC–9, the PPSAs and the Security Interests (Jersey) Law 2012, where no checking is carried out at the time of registration, there is a power for the registrar to remove frivolous or vexatious data.[5]

Inaccuracy attributable to the Keeper

9.5 The assignations record, or indeed the archive record, could be inaccurate due to the Keeper's computer system malfunctioning or a mistake being made by the Keeper's staff. For example, a fault in the system could result in an entry being deleted. The fault in theory could be as a result of hacking. Earlier we recommended that the Keeper should be required to take such steps as appear reasonable to her to protect the register from interference, unauthorised access, or damage.[6]

Reduction of assignation document

9.6 The assignation document which has been registered might subsequently be set aside by a court, for example because it has been induced by fraud or undue influence. Moreover, a court might declare the assignation document to be void from the outset on the basis that it is a forgery or was granted because of force and fear.

Should there be a correction procedure?

9.7 It would be possible to treat the Register of Assignations like the Books of Council and Session or the Register of Sasines, which are deeds registers with no procedure for corrections. But we do not think that such an approach would be satisfactory. As mentioned already, the RoA would be an automated register with no manual involvement of the Keeper's staff at the time of registration. Unlike in these other registers, it is the applicant who is responsible for the summary of the document being registered and not the Keeper. Where an assignation has been mistakenly or even maliciously registered against the wrong person there needs to be a mechanism to enable that person to clear the record of that entry. This is particularly important given that entries in the assignations record, unlike inhibitions,[7] do not lapse after five years.

Types of correction

9.8 We think that five main types of correction can be identified. First, data in an entry could be removed. For example, the entry in the assignations record might state that Grant and Helen are co-assignors, whereas in truth Grant is the sole assignor. A correction would

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[3] Land Registration (Scotland) Act 1979 s 4(2)(c). Another example of "frivolous or vexatious" in Scottish legislation is the High Hedges (Scotland) Act 2013 s 5(1)(b).

[4] LR(S)A 2012 ss 23(1)(b), 25(1)(a) and 26(1)(a). For discussion, see Scottish Law Commission, Report on Land Registration (Scot Law Com No 222, 2010) paras 12.47–12.51 and Reid and Gretton, *Land Registration* para 8.7.

[5] For example, NZ PPSA 1999 s 170, Australian PPSA 2009 s 184 and the Security Interests (Jersey) Law 2012 art 80(2).

[6] See para 6.31 above.

[7] Inhibition is a form of diligence (execution) against land. An inhibition requires to be registered in the Register of Inhibitions and Adjudications (known also as the Personal Register.)

enable Helen's details to be removed. Secondly, an entry could be removed from the assignations record to the archive record. This might happen after an assignation has been set aside by the court. Thirdly, data or a copy document in an entry might be replaced. For example, an error in the Keeper's computer system leads to Kirsten being stated as the assignor in an entry whereas it should be Jane. Fourthly, data or a copy document could be restored, for example where it has been deleted in error by the Keeper's computer system. Fifthly, an entry could be restored, for example, where the Keeper's computer system deleted it by mistake.

9.9 We consider that it would be helpful to set out the principal forms of correction in the draft Bill. We recommend:

> **39. Except in so far as the context otherwise requires, any reference to "correction" should include correction by:**
>
> **(a) the removal of data included in an entry,**
>
> **(b) the removal of an entry from the assignations record and the transfer of that entry to the archive record,**
>
> **(c) the replacement of data, or of a copy document, included in an entry,**
>
> **(d) the restoration of data, or of a copy document, to an entry,**
>
> **(e) the restoration of an entry (whether or not by removing it from the archive record and transferring it to the assignations record).**
>
> (Draft Bill, s 31(1))

How a correction is to be effected

Keeper's role

9.10 In considering how corrections should be effected we are influenced by the fact that an assignation is a *transfer*, rather than under UCC–9 and the PPSAs where "interests" are registered. Removing an "interest" from the register means that it is "unperfected". The idea of the "unperfection" of a transfer, however, is incoherent.

9.11 Moreover, one of the main purposes of registering assignations in the RoA is publicity. Third parties should be able to find a registered assignation document by searching against the assignor. That purpose would be defeated if an assignee, having registered an assignation document, had complete freedom to remove the entry by means of a correction or even to change the assignor's name.

9.12 We therefore consider that a correction should only be made by the Keeper. Borrowing from section 80 of the Land Registration etc. (Scotland) Act 2012 the Keeper should be required to make the correction where she becomes aware of a manifest

inaccuracy in the assignations record and what is needed to do to correct it is manifest.[8] If what is needed to correct the record is not manifest the Keeper should have to note the inaccuracy on the entry. The "manifest" test relates to whether it is clear that there is an inaccuracy. In contrast, the "seriously misleading" test described in Chapter 8 above, is a quantitative test about the extent to which the data in an entry is misleading. In some cases an inaccuracy might be manifest but not seriously misleading, for example a minor inaccuracy in a name which does not prevent an entry being retrieved by a search against that name.[9]

9.13 In practice the inaccuracy would be brought to the Keeper's attention by an interested party. We do not think that the Keeper should be expected to review the RoA proactively in an effort to find inaccuracies. This would increase the costs of running the register. We think that RoA Rules should be able to make provision as to the manner in which an inaccuracy in the assignations record may be brought to the Keeper's attention.

Examples

9.14 Some examples may assist explain as to how corrections would be made in practice.

9.15 Example 1. Amy grants an assignation document in favour of Brian. Brian registers this but by mistake states in the application for registration that the assignor is Carol and not Amy. Brian subsequently notices the mistake and applies to the Keeper for correction of the entry. The inaccuracy is manifest because the assignor's details in the entry do not match the copy assignation document that has been registered. If the Keeper is satisfied from the terms of Brian's application for correction that it is manifest that the entry should be corrected to replace Carol's details with Amy's then the Keeper must make the correction.

9.16 Example 2. Same as example 1, but this time Brian completes the application correctly, but unfortunately registers the wrong copy document. The inaccuracy is manifest because the assignor's details in the entry do not match the copy document that has been registered. If the Keeper is satisfied from the terms of Brian's application for correction that it is manifest that the entry should be corrected to replace the copy document then she must make the correction.

9.17 Example 3. A famous politician discovers that there is an entry in the RoA bearing to be granted by him in favour of Mickey Mouse, The Magic Kingdom, Florida. This is a vexatious registration which means that a search against the politician in the RoA would not retrieve a nil result and there may be implications for his credit rating. The politician informs the Keeper. Here it is manifest that there is an inaccuracy and equally manifest that the RoA should be corrected to remove the entry.

9.18 Example 4. The Keeper's computer system malfunctions and copy assignation documents are deleted from entries. The Keeper becomes aware of the problem. It has resulted in manifest inaccuracies in these entries because they no longer contain the copy documents. By means of a back-up system, the Keeper restores the documents. It might

[8] LR(S)A 2012 s 80(3) provides that where what is needed to rectify the register is not manifest the Keeper must enter a note identifying the inaccuracy or in the cadastral map.
[9] This of course would depend on the programming of the searching software. See paras 10.22–10.29 below.

be that in some circumstances of computer malfunction that it would take time for the Keeper to retrieve the relevant data or copy document from the back-up system and therefore it is not manifest immediately as to what is to be done. Here the Keeper would meantime note the inaccuracy in the entry.

9.19 It would take the Keeper some time to consider an application for correction. Therefore to protect their priority we expect that an assignee who notices a mistake may re-register the assignation immediately using the automated system before applying for correction. In that case the correction sought may simply be to remove the bad entry rather than to alter it. It might be possible for a system to be devised whereby an application for registration could be accompanied by an application for correction by means of removal.

Effecting a correction

9.20 Where a correction involves removing the entire entry which would be the case typically with a frivolous or vexatious registration, the Keeper should have to transfer the entry to the archive record and to note the reason for the correction and its date and time. If a correction merely involves correcting data or a copy document, the entry would not of course go to the archive record, but once again the details and the date and time of the correction should be required to be noted. In the case of replacing a copy document which is incorrect, the removed document should be transferred to the archive record.

9.21 We think that the Keeper when making a correction should be required to notify those who are specified in RoA Rules as being entitled to receiving notification. We expect that the rules would specify the parties to the assignation document which has been registered and probably any party named in the entry prior to the correction, such as a person erroneously named as assignor when in fact they were not. We think that the Keeper should also be entitled to notify any other person to whom she thinks that notification should be made.

9.22 We recommend:

40. (a) Where the Keeper becomes aware of a manifest inaccuracy in an entry in the assignations record the Keeper should have to correct the inaccuracy if what is needed to correct it is manifest. If what is needed to correct is not manifest the Keeper should have to note the inaccuracy on the entry.

(b) Where an inaccuracy is corrected by:

(i) removal of the entry the Keeper should have to transfer the entry to the archive record and note on the entry the details of the correction, and its date and time,

(ii) removal or replacement of data included in the entry or by replacement of a copy document the Keeper should have to note on the entry the details of the correction, and its date and time,

(iii) replacement of a copy document, the Keeper should have to transfer it to the archive record.

(c) Where the Keeper effects a correction, the Keeper should have to notify each person specified for these purposes by RoA Rules and any other person whom the Keeper considers it appropriate to notify that the correction has been effected.

(Draft Bill, s 28)

Correction of the assignations record by order of a court

9.23 The Keeper cannot be expected to act quasi-judicially and decide, for example, that the assignation document is a forgery. Such matters must be for a court. We consider therefore that a court should be able to determine that the assignations record is inaccurate and require the Keeper to correct it. For example, an assignation document might be determined by a court to be a forgery. Alternatively, there might be court proceedings which result in an entry becoming inaccurate. For example, an assignation might be reduced by a court on grounds such as fraud, or facility and circumvention. Equally, an assignation might be reduced in part as regards a co-assignor. It is important in such circumstances that the entry or data can be removed from the assignations record so that a search against the purported assignor would not retrieve it.

9.24 We consider that where the court directs the Keeper to correct, it should also be able to give the Keeper further direction, for example as to how and when the correction is to be made.

9.25 In the case of the entry being removed, or a copy document being removed because it is replaced with the correct document, the entry or document would be transferred to the archive record.[10] In the case of only data being removed or replaced the Keeper should have to note the details of the correction, including its date and time in the entry.

9.26 Where the Keeper makes a correction following a direction from the court, the Keeper should be required to notify the persons specified for these purposes by RoA Rules and any other person who the Keeper considers it appropriate to notify. We would expect RoA Rules to require notification to the persons identified as the assignor and as the assignee in the relevant entry.

9.27 We recommend:

41. (a) Where a court determines that the assignations record is inaccurate it should have the power to direct the Keeper to correct it.

(b) In connection with any such correction, the court should be able to give the Keeper such further direction (if any) as it considers requisite.

[10] See paras 11.19–11.21 below.

(c) The Keeper should be required to note on the relevant entry that it has been corrected and the details of the correction, including the date and time. Where the correction requires the removal of the entry or of a copy document the Keeper should have to transfer it to the archive record.

(d) Where the Keeper effects a correction, the Keeper should have to notify each person specified for these purposes by RoA Rules and any other person whom the Keeper considers it appropriate to notify that the correction has been effected.

(Draft Bill, s 29)

Keeper's right to appear and be heard in proceedings in relation to inaccuracies

9.28 Section 83 of the Land Registration etc. (Scotland) Act 2012 provides that the Keeper has the right to be appear and be heard in relation to any proceedings concerning the accuracy of the Land Register or concerning what is needed to rectify an inaccuracy in that register. We think that there should be a similar rule as regards inaccuracies in the RoA.

9.29 We recommend:

42. The Keeper should be entitled to appear and be heard in any civil proceedings, whether before a court or tribunal, in which is put in question (either or both):

(a) the accuracy of the assignations record,

(b) what is needed to correct an inaccuracy in that record.

(Draft Bill, s 30)

Effect of correction

9.30 A correction is the means by which the RoA is amended to reflect the true legal position. Some corrections would be to *remove* incorrect entries or data, for example where an entry was based on a forged assignation or there was a registration which was frivolous or vexatious. Here the correction has no effect on the assignation because there has never been a valid assignation. Sometimes there may have been an assignation which although valid is voidable, perhaps because of fraud. If the court reduces the assignation the transfer of the claim is rendered ineffective. In such circumstances we would expect that the court would also order the correction of the RoA to remove the relevant entry under the powers which we recommend above.

9.31 In other cases, a correction may involve *replacement* of data or a copy document in an entry. For example, the entry states incorrectly that Amy has assigned in favour of Boris, but the assignation document is by Charles in favour of Boris. The Keeper corrects the entry to replace Amy's name with Charles's. The result must be that the registration becomes effective because there is no longer a seriously misleading inaccuracy. The claim held by Charles is duly transferred to Boris. The correction has substantive effect.

9.32 We recommend:

43. A registration which is ineffective should become effective if and when the entry is corrected.

(Draft Bill, s 26(3))

Date and time of correction

9.33 In the same way as the register states the date and time that an assignation document is registered, it should also state the date and time of correction. This is particularly important in circumstances where the correction has substantive effect, in other words makes an ineffective registration effective.

9.34 We recommend:

44. A correction should be taken to be made on the date and at the time which are entered for it in the register.

(Draft Bill, s 31(2))

Chapter 10 Register of Assignations: searches and extracts

Searches

10.1 One of the principal policy reasons for having a Register of Assignations is so that it can be searched against particular persons to check whether they have granted an assignation.[1] It is therefore self-evident that the RoA requires an effective searching mechanism. Searches would of course be made electronically under the automated system and would not require the involvement of the Keeper's staff.

What can be searched?

10.2 An entry in the RoA would consist of (a) data and (b) the copy assignation document. In theory a search mechanism could be set up where any words could be searched against in both data and documents. For example, a search against "Robert Burns" would retrieve any entry where that name is mentioned, as an assignor, an assignee, an account debtor or even in a street name in one of the parties' addresses. This has the potential for a very cluttered search result. A far more preferable approach, in our view, is to restrict the search to certain data which would have been entered in the application for registration and which would therefore form part of the entry data.

10.3 The RoA would be a person-based register and therefore would principally be searched by reference to a person: the assignor. In line with the position under UCC–9 and the PPSAs we do not recommend that searches can be made against assignees. The reason for this is that it would provide too easy a way for a competitor to discover the details of a financial institution's clients.[2] Clearly, it also does not make sense for searches to be made directly against categories of claims, for example "rents", as a voluminous number of search results would be returned.

10.4 In relation to searches against assignors, we think that there should be three possibilities as regards data that can be directly searched against. The first would be by reference to the assignor's name. A search against "Augustus Brown Collins" should retrieve any entry in which Augustus Brown Collins is named as an assignor or as a co-assignor. Earlier, we recommended that RoA Rules set out the "proper name" of an assignor for the purposes of registration which would allow there to be certainty as to how a name should be stated.[3]

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[1] Alternatively, enquiries can be made with the debtor to see if an assignation has been intimated to them. But where there is no identifiable debtor, as is typically the case with a future claim, intimation is impossible.

[2] Although in the interests of flexibility we recommend below at para 10.10 a provision allowing the register to be searched by other factors or characteristics prescribed in RoA Rules and the assignee's details could become directly searchable if prescribed in this way. And where a retrocession of an assignation in security is registered the assignor would typically be a financial institution. See paras 7.43–7.47 above.

[3] See paras 7.5–7.6 above.

10.5 The second possibility would be by references to *both* the name and date of birth for assignors who are individuals. A search against date of birth only should not be possible. Such a search should lead to a less cluttered result than a search against name only. Where the assignor's name is a common one such as "John Smith" this is more important than in less usual names such as "Augustus Brown Collins". As noted elsewhere, we are aware that the presence of dates of birth on a public register raises privacy issues, but we think that there are ways to deal with this.[4]

10.6 The third possibility would be by reference to the unique number of the assignor where the assignor is a person required by RoA Rules to be identified in the assignations record by such a number. We have in mind in particular UK companies and LLPs.[5] Using such numbers has two benefits: they are precise and unlike, for example, a company's name, they do not change.

10.7 We considered whether it should also be possible to search against name and address, but we decided against this principally because (a) the same address can be expressed in different ways (for example, 140/1 Causewayside or Flat 1, 140 Causewayside) and (b) addresses are more likely to change than names.[6] While therefore name and address could not be the subject of a direct search, an entry once found by means of, for example a name search, could be used as additional evidence that the relevant person has been found.

10.8 We think that it should also be possible to search the assignations record by reference to the unique number for an entry (which would depend on the searcher knowing that number) and by reference to any other factor or characteristic specified by RoA Rules.

10.9 The result of carrying out a search against particular data would be to retrieve all entries containing that data. For example, if Andrew Baxter has granted an assignation of his patent royalties to the Cornhill Bank and an assignation of his shop rents to the Deveron Bank, and both assignations have been registered, a search against him would retrieve both assignation entries.

10.10 We recommend:

45. The assignations record should be searchable only

(a) by reference to any of the following data in the entries contained in that record:

(i) the names of assignors,

(ii) the names and dates of birth of assignors who are individuals,

[4] See para 7.9 above.
[5] Cf LR(S)A 2012 s 113(1) (definition of "designation").
[6] Cf Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 523.

(iii) the unique numbers of assignors required by RoA Rules to be identified in the assignations record by such a number,

(b) by reference to registration numbers allocated to entries in that record, or

(c) by reference to some other factor, or characteristic, specified for these purposes by RoA Rules.

(Draft Bill, s 32(2))

Who can search?

10.11 Some registration systems restrict the categories of persons who can search the register in order to protect the privacy of parties whose details are registered. For example, the German Land Register (*Grundbuch*) has a requirement of "legitimate interest" before a search can be made.[7] In the New Zealand Personal Property Securities Register searches can only be made by a restricted number of persons for a restricted number of purposes.[8] A breach of these rules gives rise to an action for breach of privacy.[9]

10.12 We noted in the Discussion Paper that while privacy considerations are relevant, the logic of registration is publicity and not privacy.[10] A strong privacy agenda would impact on the value of the system. For example, a rule that a search against a person can only be carried out with that person's permission would increase transaction costs. The UNCITRAL Legislative Guide states: "The information provided on the record in the registry is available to the public. A search may be made without the need for the searcher to justify the reasons for the search."[11]

10.13 In our Report on Land Registration we commented on the fact that public registration has a long history in Scotland.[12] Land transactions have now been viewable to the public for four hundred years since the Registration Act 1617. Clearly, however, the digital revolution means that information is much more easily obtainable and there is a view that a more restrictive approach should now be taken to what data should be available to the public by means of a search.[13] A balance between publicity and privacy needs to be achieved. As the South African Constitutional Court has noted: "Privacy, like other rights, is not absolute. As a person moves into communal relations and activities such as business and social interaction, the scope of personal space shrinks."[14]

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[7] § 12 Grundbuchordnung.
[8] NZ PPSA 1999 s 173. See Allan, *The Law of Secured Credit* 478–479.
[9] NZ PPSA 1999 s 174. We understand that this provision has rarely if ever been used. See also the Australian PPSA 2009 s 173.
[10] Discussion Paper, para 20.31.
[11] UNCITRAL Legislative Guide para 55.
[12] Scottish Law Commission, Report on Land Registration (Scot Law Com No 222, 2010) vol 1 para 8.24.
[13] See A Berlee and J Robbie, "Publicity and Privacy in Land Reform in Scotland" (24 September 2015) available at http://schooloflaw.academicblogs.co.uk/2015/09/24/publicity-and-privacy-in-land-reform-in-scotland/.
[14] *Gaertner v Minister of Finance* 2014 (1) SA 442 (CC) para 49. See also *Nova Group v Cobbett* (2016) 4 SA 317.

10.14 The data which would appear in the assignations record would be relatively limited and principally consist of the name and address of the assignor and assignee. Often these parties would be partnerships, companies, LLPs or other corporations rather than private individuals.

10.15 While, as already mentioned,[15] we think that the dates of births of assignors who are individuals should require to be registered, RoA Rules could provide for the RoA to be set up in a way whereby the date of birth is either partially or entirely hidden.[16] In relation to the assignation document we recommend elsewhere that RoA Rules should be able to specify that information in it or signatures can be redacted as is the position for registration of charge documents in the Companies Register.[17] We think that limiting what is available to the searcher is a simpler way of proceeding than limiting the classes of person who can search the RoA.

10.16 It should also be possible for RoA Rules to set out requirements in relation to searches, for example as to the information which the person requesting the search must supply. Finally, it would be necessary for a fee to be paid to the Keeper. The fees would contribute to the costs of establishing and running the RoA. Having to pay a fee may also deter those who have no particular reason for searching.

10.17 We recommend:

46. A person should be able to search the assignations record if the search accords with RoA Rules and either the appropriate fee is paid or the Keeper is satisfied that it will be paid.

(Draft Bill, s 32(1))

Data protection

10.18 The information which would be kept in the RoA would, as considered above, include the name and address of the assignor and assignee, and the date of birth of an assignor who is an individual.

10.19 The name, address and date of birth of a living individual are all the personal data of that individual for the purposes of the Data Protection Act 1998[18] (the "DPA"). The DPA protects the privacy of such individuals by regulating the manner in which a data controller such as the Keeper can process the data, and by giving the individual rights to information and to control over processing in certain circumstances.

10.20 The DPA also provides for various public interest exemptions from rights and duties under that Act. Section 34 of the DPA sets out that personal data are exempt from key controls if the data consists of information which the data controller is obliged by or under an

[15] See para 10.5 above.
[16] See paras 7.7–7.9 above.
[17] See para 11.46 below.
[18] The 1998 Act transposes Directive 95/46/EC (OJ L 281, 23.11.1995, p 31). The Data Protection Directive will be replaced from the 25 May 2018 by Regulation (EU) 2016/679 (OJ L 119, 4.5.2015, p 1). The new EU General Data Protection Regulation will be directly applicable in the UK legal order, and will make substantial changes to the EU data protection regime. We have not considered the effect of those changes in this Report.

enactment to make available to the public (whether or not on payment of a fee). That exemption would apply as appropriate to the Keeper when exercising her functions under the legislation governing the RoA.

10.21 The effect of the exemption is that disclosure of information is regulated by the appropriate enactment, to the extent that the exemption is engaged. It follows that the proposed registration scheme should have due regard for the privacy of living individuals whose private information would be held on the RoA. We considered this issue above.[19]

Search facilities

10.22 In the UCC–9 and PPSA registers a general distinction is recognised between "exact match" and "close match" searching. An "exact match" search only retrieves exact matches of the search terms (subject to the basic search logic). For example, a search against "Katharine Smith" will not find an entry against "Katherine Smith". This means that the party making the registration has to achieve almost complete accuracy.[20] A small typographical error is all that is needed for the registration to be ineffective.[21]

10.23 In contrast, "close match" searching uses search logic which finds words which are similar to the target name. The degree of latitude depends on the programming of the system. Under this system a search will retrieve a greater number of results relating to names similar to the target name, most of which will be irrelevant. The searcher therefore has to differentiate between relevant and irrelevant (or what is sometimes termed "false positive") results. Hence the leniency granted to the party making the registration has the consequence of requiring more effort on the part of the searcher.

10.24 Exact match searching is used in Ontario, New Zealand and Australia, whereas the other Canadian provinces with PPSAs use close match searching.[22] To some extent this policy choice has been driven by the size of the jurisdiction. In larger jurisdictions with the potential for more results, an exact match approach seems preferable. Yet New Zealand, which has a similar population size to Scotland and one smaller than Australia and Ontario, has an exact match system. It must be remembered, however, that the number of registrations in a functional system of security interests will be far higher than under our scheme, where only assignations would be registered in the RoA.

10.25 In New Zealand there is also the possibility of a "wild card" search where the end of a word is replaced with an asterisk. For example, a search against "Ian Thom*" will retrieve an entry against Ian Thomson or Ian Thompson, but not Ian Timpson.[23]

10.26 Under any of these systems of searching, the search logic depends precisely on how the computer system is programmed in the particular register. For example, a search need not be case-sensitive and thus not distinguish between upper and lower case letters.

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[19] See paras 10.11–10.17 above.
[20] There is a little latitude depending on the search logic of the computer system. See para 10.26 below.
[21] See generally *Polymers International Ltd v Toon* [2013] NZHC 1897.
[22] See Cuming, Walsh and Wood, *Personal Property Security Law* 364-366; Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 473–474; M Gedye, "The New Zealand Perspective" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 115 at 135–136.
[23] Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 481–483; Allan, *The Law of Secured Credit* 480–481.

Searches against "&" can be set up to find "and" and vice versa. Spaces, punctuation marks and accents can be disregarded. So too can abbreviations at the end of a legal person's name that indicate the nature of the person (LLP, Ltd etc).

10.27 There is a close inter-relationship between the search facility and the "seriously misleading" test in the UCC–9 and PPSA jurisdictions. If an error results in the entry not being retrieved by a search the error will be regarded as seriously misleading and the registration will be ineffective. In Chapter 8 above we recommended that this test is also used in the RoA. We also concluded there that the matter of whether an "exact match" or "close match" approach should be one which is discussed with stakeholders when the Register is being set up. Clearly, the former is more demanding on the person registering because a small error may result in the entry not being retrieved by a search and the registration is thus invalidated on the basis that there is a "seriously misleading" error. But, the benefit of such an approach, is that a search result is less cluttered as it only returns "exact" and not "close" matches.

10.28 We think that the Keeper should have to provide a search facility for the purposes of the "seriously misleading" test. In shorthand, this might be referred to as the "official" search facility. Its criteria, in other words the criteria in accordance with which what is searched for must match data in an entry in order to retrieve that entry, would be specified by RoA Rules. In practice we would expect it to be either "exact match" or "close match". But we think that it should also be possible for the Keeper to offer alternative search facilities, for example "wild card" searching.

10.29 We recommend:

47. (a) The Keeper should be required to provide a search facility in relation to which the search criteria are specified by RoA Rules, but may provide such other search facilities, with such other search criteria, as the Keeper thinks fit.

(b) "Search criteria" should be defined as the criteria in accordance with which what is searched for must match data in an entry in order to retrieve the entry.

(Draft Bill, s 33)

Printed search results

10.30 While the RoA would exist in electronic form it would be possible to print a copy of a search result. We think that the result should be admissible in evidence before a court. In addition, unless there is contrary evidence it should be capable of proving the registration of the assignation document to which the result relates, a correction of the entry in the assignations record to which the result relates, and the date and time of the registration or

correction.[24] If its authenticity were challenged, the solution would be to seek a formal extract from the Keeper under the recommendations which we make below.

10.31 We recommend:

48. A printed search result which purports to show an entry in the assignations record should be admissible in evidence, and in the absence of evidence to the contrary, should be sufficient proof of:

(i) the registration of the assignation document to which the result relates,

(ii) a correction of the entry in the assignations record to which the result relates, and

(iii) the date and time of such registration or correction.

(Draft Bill, s 34)

Extracts

10.32 As in the Land Register we think that it should be possible for application to be made to the Keeper for a formal extract of an entry.[25] This would include an entry which has been moved to the archive record following a correction, although such cases would be rare.[26] There would of course be a fee payable. We think that the Keeper should be allowed to authenticate the extract as the Keeper considers appropriate.[27] Since the RoA is to operate electronically, we consider that the Keeper should be able to issue the extract as an electronic document unless the applicant requests a traditional (paper) document.[28] As is the case under the land registration legislation we think the extract should be accepted for all purposes as sufficient evidence of the contents of the entry.[29] The extract would be time-sensitive given that it would be possible for entries to be changed by means of a correction.[30]

10.33 Elsewhere we recommend that RoA Rules may permit the Keeper to exclude certain information appearing in the register from an extract.[31] We have in mind privacy concerns. We also deal with the Keeper's liability for incorrect extracts below.[32]

10.34 We recommend:

49. (a) Any person should be able to apply to the Keeper for an extract of an entry in the register.

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[24] We have been influenced here by the equivalent provisions in the PPSAs. See eg Saskatchewan PPSA 1993 s 48(2) and NZ PPSA 1999 s 175. And see the Security Interests (Jersey) Law 2012 art 84.
[25] See LR(S)A 2012 s 104.
[26] See Chapter 9 above.
[27] Cf LR(S)A 2012 s 104(6).
[28] On traditional documents, see the Requirements of Writing (Scotland) Act 1995 s 2.
[29] LR(S)A 2012 s 105(1).
[30] See Chapter 9 above.
[31] See para 11.46 below.
[32] See para 11.29 below.

(b) The Keeper should be required to issue the extract if the appropriate fee is paid or the Keeper is satisfied that it will be paid.

(c) The Keeper should be able to validate the extract as the Keeper considers appropriate.

(d) The Keeper should be able to issue the extract as an electronic document if the applicant does not require that it be issued as a traditional document.

(e) The extract should be accepted for all purposes as sufficient evidence of the contents, as at the date on which and the time at which the extract is issued (being a date and time specified in the extract), of the entry.

(Draft Bill, s 35)

Chapter 11 Register of Assignations: other issues

Introduction

11.1 In this chapter we consider miscellaneous matters in relation to the register, namely (1) information duties; (2) duration of registration and decluttering; (3) archiving; (4) the liability of the Keeper and other parties for errors and breach of duties; and (5) RoA Rules.

Information duties

Introduction

11.2 The information which would appear in entries in the RoA would not always be comprehensive. This is true even although a copy of the assignation document appears in the entry. For example, an assignation may be of future invoices specified in schedules to be sent from the assignor to the assignee.[1] Thus the register by itself would not reveal whether a particular invoice has been assigned. Another possibility is that the assignation document contains a suspensive condition. The register would not reveal whether the condition has been purified.

11.3 Under UCC–9,[2] the PPSAs,[3] the DCFR,[4] the Security Interests (Jersey) Law 2012[5] and the UNCITRAL Model Law on Secured Transactions[6] the issue that the register only provides notice of a secured transaction[7] and thus very limited information is addressed by imposing information duties on the party that has registered the notice. Under some of these systems only the debtor is entitled to off-register information and therefore a third party would have to obtain the information via the debtor. But under others some third parties have independent rights.[8]

11.4 The RoA is not a notice filing register but rather a register where documents are filed. More information would therefore be directly obtainable from it than from a notice filing register. Nevertheless, we consider that there should be *limited* statutory information duties owed to a *limited* number of third parties. Such an approach seeks to draw a balance between the fact that neither the details of individual claims being assigned nor information that a suspensive condition has been purified require to appear on the register.

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[1] See paras 4.27–4.28 above.
[2] UCC § 9–210.
[3] Eg NZ PPSA 1999 ss 177–183. See Allan, *The Law of Secured Credit* 481–482.
[4] DCFR IX.–3:319 to 3:324.
[5] Security Interests (Jersey) Law 2012 art 85.
[6] UNCITRAL Model Law on Secured Transactions art 56.
[7] Or even merely the possibility of a secured transaction.
[8] Under UCC–9 the rights extended to the debtor only. But under the PPSAs third parties have rights. See C Walsh, "Transplanting Article 9: The Canadian PPSA Experience" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 49 at 66–67. Similarly, the Jersey legislation is limited to the debtor but not the DCFR.

What information?

11.5 We think that the information which could be requested should be relatively limited. A third party should only be able to ask whether a particular claim is assigned by the assignation or whether a condition to which the assignation is subject has been satisfied. It should not be possible simply to ask for a list of all the claims that have been assigned. The starting point should be that the third party identifies the claims in respect of which the information is sought. Example. B Ltd, a multi-trades company, grants an assignation to the Crimond Bank of future invoices specified in schedules to be sent from B Ltd to the Crimond Bank. An information request could be made as to whether, for example, the invoices issued in May 2022 have been listed in such a schedule.

Who can request?

11.6 Only a limited category of persons should be entitled to make a request, namely those who are affected or potentially affected by the assignation. The approach taken in the DCFR is that any party may make a request to the secured creditor if they have the consent of the provider of the security.[9] We recommend that a similar approach is taken with regard to the RoA and that third parties may make a request if they have the permission of the person identified in the entry as the assignor. For example, B Ltd, a multi-trades company, grants an assignation to the Crimond Bank of future invoices specified in schedules to be sent from B Ltd to the bank. B Ltd and the Crimond Bank subsequently agree that only invoices for plumbing work will be assigned. A few months later B Ltd enters into negotiations with the Duffus Bank about assigning its invoices for electrical work. The Duffus Bank searches the RoA and discovers the assignation. B Ltd advises that the arrangement is only for plumbing invoices. With B Ltd's permission, the Duffus Bank is entitled to have the Crimond Bank confirm this.

11.7 We consider that certain persons should also have independent rights to request information. We have in mind, first, a person who has a right to execute diligence against the claim, even if a charge for payment has not yet been executed.[10] There is a difficulty here. Whether a person has the right to execute diligence depends on who holds the claim. If it is held by the assignor then that party's creditors would be entitled to do so. If it is now held by the assignee then it would now be the assignee's creditors who would be so entitled. It is only on being supplied with the information as to who holds the claim that the requester will know the position. Therefore we consider that both creditors of the person identified in the entry as the assignor and as the assignee should be able to make a request.

11.8 Secondly, we think that there should be power to prescribe other categories of person who would be entitled to make an information request. We have in mind insolvency officials and executors.

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[9] DCFR IX.–3:319(1).

[10] Such a right is recognised under several of the PPSAs. See eg NZ PPSA 1999 s 177(1) ("judgment creditors") and the Australian PPSA 2009 s 275(9)(d).

How should a request be made?

11.9 The request should require to be made to the person identified as the assignee in the entry. In theory it could be made orally but we would expect it would normally be made by electronic communication.

11.10 We recommend:

> **50. (a) An entitled person should be entitled to request from the person identified in an entry in the assignations record as the assignee a written statement as to:**
>
> **(i) whether or not a claim specified in the notice is assigned; or**
>
> **(ii) whether a condition to which the assignation is subject has been satisfied.**
>
> **(b) The following should be entitled persons:**
>
> **(i) a person who has the right to execute diligence against a claim specified in the notice (or who is authorised by decree to execute a charge for payment and will have the right to execute diligence against that claim if and when the days of charge expire without payment) depending on whether the claim has been assigned by the assignation,**
>
> **(ii) a person who is prescribed for these purposes, and**
>
> **(iii) a person who has the consent of the person identified in the entry as the assignor.**
>
> (Draft Bill, s 36(1) to (3))

Duty to comply with information requests

11.11 We think that the person identified in the entry as the assignee should have 21 days to comply.[11] But this would be subject to certain exceptions.[12] It should be possible to apply to the court to seek an extension to the 21-day period. The court should be entitled to make such an order if it is satisfied that in all the circumstances it would be unreasonable for the person to comply within that period. Relevant factors here might be difficulty in finding the information or in verifying the requester's entitlement to obtain it.[13] Similarly, it should be possible to apply to the court to be exempted from the requirement to supply the information either in whole or part, with the court once again having to be satisfied in all the circumstances that it would be unreasonable to expect the request to be complied with.

[11] The periods under comparator legislation vary. For example, under the Australian PPSA 2009 s 277 the period is 10 business days, under the NZ PPSA 1999 s 178 the period is 10 working days, under the DCFR IX.–3:319(3) the period is 14 days and under the Security Interests (Jersey) Law 2012 art 85(2) the period is 30 days.
[12] Cf NZ PPSA 1999 s 179, Australian PPSA 2009 s 278 and Security Interests (Jersey) Law 2012 s 86.
[13] Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 543.

Relevant factors here could be the reasonableness of the inquiry and the relevance of the information to the requester.[14] For example, the value of information as to long-dead claims may be doubtful.

11.12 Drawing on the DCFR,[15] we think that there should also be no requirement to comply if it is manifest from the entry that the claim in question is not assigned. For example, in the entry it is stated that the assignation is of royalties. It is therefore directly apparent that the assignation is not of rents and therefore an information request querying whether rents are included can be ignored. Moreover, if the same requester has made the same request within the last three months and nothing has changed since then, there should be no requirement to comply.

11.13 Similarly, there should no need to comply if it is manifest that the registration is ineffective. For example, an entry states that Clarissa is the assignor and the Barra Bank is the assignee. But the copy document which has been registered is an assignation by Colin in favour of the Barra Bank. In such a case it is patent that no claim has been transferred because the registration has been botched and no information need be supplied.

11.14 It has been suggested to us by our advisory group that the assignee should also be able to decline to answer the request if the assignee does not hold the relevant information. We understand that in some invoice financing transactions the assignor continues to hold the ledger of relevant invoices and therefore it has the relevant information rather than the assignee. We consider, however, that in such circumstances the assignee should obtain the information from the assignor or authorise the assignor to provide it to the party making the request.

11.15 If none of the exceptions apply and the person identified in the entry fails to supply the requested information it should be possible for the entitled person to seek an order requiring them to do so within 14 days. We think that the court should make such an order if it is satisfied that the registered assignee has failed to comply without reasonable excuse. Failure to adhere to the order would be contempt of court. Elsewhere we recommend also statutory liability to any party who has suffered loss as a result of failure to comply with the information duty requirements without reasonable excuse.[16]

Cost of complying with request

11.16 We think that the registered assignee should be entitled to recover the reasonable costs of providing the information.[17]

11.17 We recommend:

51. (a) An information request should require to be complied with within 21 days of its receipt, unless:

[14] Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 543.
[15] DCFR IX.–3:320(5).
[16] See paras 11.35–11.42 below.
[17] NZ PPSA 1999 s 180(1); Australian PPSA 2009 s 279(1).

(i) a court is satisfied that in all the circumstances this would be unreasonable and either extends the 21-day period or exempts the recipient from complying with the request in whole or in part,

(ii) it is manifest from the entry that the claim specified in the notice has not been assigned by the assignation document or that the registration is ineffective, or

(iii) the same request has been made by the same person within the last 3 months and the information supplied in response to the last request has not changed.

(b) The recipient should be entitled to recover from the requester any costs reasonably incurred in complying with the request.

(c) If a court is satisfied on the application of the requester that the recipient has not complied with the duty to provide information without reasonable excuse it should by order require that the recipient complies within 14 days.

(Draft Bill, s 36(4) to (8))

Duration of registration and decluttering

11.18 In the Discussion Paper we considered whether as in UCC–9/PPSA systems there should be a lapsing provision, under which a registration ceases to be effective after a certain period unless renewed.[18] This helps declutter the register, making it easier to search. That discussion, however, was in the context of security rights rather than assignations. The concept of a duration does not fit well with an assignation being a transfer, even although claims are ephemeral and often have short lives. We recommend no lapsing provision for assignations.

Archiving

11.19 We noted earlier in the Report that consultees supported archiving.[19] But archiving in the context of assignations would be relatively unusual and be limited to whether the assignations record is incorrect. This can be contrasted with the position for the new security (the statutory pledge) which we recommend later in this Report. There needs to be the facility for it to be removed from the active part of the register and archived where it is extinguished.[20] A search against a person in the register should show security rights which are extant. An assignation, however, being a transfer, is never extinguished.[21]

11.20 Nevertheless, where the register is corrected to remove an entry we think that the Keeper should be required to transfer it to the archive record. The archive record would

[18] Discussion Paper, paras 20.51–20.53.
[19] See para 7.2 above.
[20] See Chapters 23 and 33 below.
[21] What is likely to be extinguished is the claim as claims are typically ephemeral.

therefore be made up of the totality of all such transferred entries. RoA Rules might specify further information that requires to be noted by the Keeper.

11.21 We recommend:

52. The archive record should be the totality of all the entries transferred from the assignations record following a correction and include other data specified by RoA Rules.

(Draft Bill, s 22)

Liability of Keeper and other parties

Introduction

11.22 In certain situations we think that there should be statutory liability imposed on the Keeper for losses caused by Keeper-error in relation to the running of the register and the supply of incorrect information. In addition, we think that there should also be liability imposed on a party who has registered an assignation for losses caused by errors in the registered data or failure to comply with the information duties which we have recommended. Liability provisions can be found under UCC–9, the PPSAs and the Land Registration etc. (Scotland) Act 2012.[22]

Liability at common law

11.23 An initial question is whether there is a need to impose statutory liability or whether the matter can be left to the general law.[23] For example, where the Keeper has made an error that has caused wrong data to appear in an entry in the RoA, a person who has suffered a loss as a result of that error is likely to have a remedy in delict if negligence can be established.[24] But the position cannot be stated with certainty.[25] Difficult questions can arise as to whether a public body in carrying out statutory duties can be liable in delict in the absence of an express provision on civil liability in the relevant statute.[26] We are of the view that making express provision is the preferable option as this would offer greater certainty. In addition, as regards the Keeper, we consider that liability should be strict, which is not the position under the general law.

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[22] UCC § 9–625(b); Saskatchewan PPSA 1993 s 65(5); NZ PPSA 1999 s 176 and LR(S)A 2012 ss 84(1)(b) and 106.

[23] For a helpful discussion as regards the common law liability of the Keeper in respect of the Land Register, see Reid and Gretton, *Land Registration* paras 14.9–14.12.

[24] See *Schubert Murphy v Law Society* [2014] EWHC 4561 (QB) and *Sebry v Companies House* [2015] EWHC 115 (QB).

[25] To establish a duty of care on the part of the Keeper the claimant would probably have to satisfy the three-part test set out by Lord Bridge of Harwich in *Caparo Industries plc v Dickman* [1990] 2 AC 605 at 617H–618B: (1) the foreseeability of the damage; (2) proximity (here between the claimant and the Keeper); and (3) that it is fair, just and reasonable to impose a duty upon the defender, here the Keeper.

[26] See *X (Minors) v Bedfordshire County Council* [1995] 2 AC 633; *Gorringe v Calderdale MBC* [2004] UKHL 15; *Braes v Keeper of the Registers of Scotland* 2010 SLT 689 and *Santander UK plc v Keeper of the Registers of Scotland* [2013] CSOH 24.

Liability of Keeper

11.24 The Keeper's role is to manage the RoA. It is necessary that the register is reliable and that the data and documents registered are not affected by any inaccuracy caused by the Keeper, or more precisely the Keeper's staff and computer system. Third parties would rely on the RoA for accurate information and where that information is not accurate because of a mistake for which the Keeper is responsible we think that the Keeper's liability should be strict. This is the position under the Land Registration etc. (Scotland) Act 2012 as regards the Land Register in respect of the issuing of incorrect extracts or information.[27]

11.25 We consider that the Keeper's liability should fall broadly under four heads. First, this would be in respect of the making up, maintenance or operation of the RoA and in the attempted making of corrections. There is no direct equivalent of this head in the 2012 Act and liability in such circumstances in relation to the Land Register would necessitate the requirements of the general law being satisfied.[28] The Land Register, however, is a far more complex register than the RoA. For the most part the RoA would be automated[29] and we consider that the Keeper should have strict liability where the computer system malfunctions.[30] This would hopefully be very rare. In contrast, in relation to corrections, manual input would be needed from the Keeper's staff and there could be human error. Failure to make a correction may have serious consequences and we take the view that there should be strict liability in such circumstances too. Some examples may assist.

11.26 Example 1. An application is made to register an assignation by Fred in favour of Ginger. The entry made up by the computer system gives the name of the assignor as Frank. The result is an ineffective registration because there is a seriously misleading inaccuracy. The assignee, Ginger, should be compensated for any loss suffered.

11.27 Example 2. The computer system deletes an entry for an assignation of rents by Peter to the Rathen Bank. Peter (fraudulently) assigns the rents again to the St Cyrus Bank, who relies on the fact that a search in the RoA against Peter is clear. The St Cyrus Bank should be compensated for its loss because the computer error meant that it could not find the assignation. We consider too that the Keeper should be liable for loss suffered as a result of an attempted correction to the RoA, where in fact no correction should have taken place.

11.28 Example 3. The Keeper corrects the assignations record to remove a number of vexatious registrations against a famous politician, but mistakenly also removes a genuine entry. The assignee in relation to the genuine entry should be compensated for any loss suffered, for example by a third party challenging whether there has been such an assignation.

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[27] See LR(S)A 2012 s 106.
[28] See Reid and Gretton, *Land Registration* para 14.10.
[29] See paras 6.40–6.45 above.
[30] Other jurisdictions take varying approaches to this issue. Registrar liability in New Zealand appears to require negligence on the registrar's part: see Gedye, Cuming and Wood*, Personal Property Securities in New Zealand* 533. In some of the Canadian provinces, there is no liability on the registrar where the electronic system fails to effect the registration or to effect it satisfactorily. See Cuming, Walsh and Wood, *Personal Property Security Law* 372. Such an approach seems harsh on the party making the registration.

11.29 Secondly, we consider that the Keeper should be liable for the provision of incorrect information in a verification statement, or an extract which is not a true extract.[31] Thus where the Keeper issues a statement verifying that an assignation document has been registered the recipient should be able to rely on that and have a remedy for loss suffered for example where in fact no entry has been made up.

11.30 Thirdly, the Keeper should be liable where a notification issued in relation to a correction of the register is itself incorrect, for example it states that the correction has been made when it has not.

11.31 As under the 2012 Act,[32] we think that the Keeper's statutory liability should be subject to the duty of the party claiming compensation to mitigate their loss. For example, where a claim is made in respect of loss suffered by an incorrect entry the claimant would be expected to have drawn this to the Keeper's attention as soon as is reasonably possible so that it can be corrected and the loss minimised.

11.32 We consider also that there should be no liability for loss that is not reasonably foreseeable. The wording in the 2012 Act is "in so far as a claimant's loss is too remote"[33] but the role of remoteness in the Scots law of delict is a matter on which at least on one view there is now uncertainty.[34] A "reasonably foreseeable" test is typically found in the PPSAs.[35]

11.33 Finally, again as with the position in respect of the Land Register we are of the view that there should not be liability for non-patrimonial loss.[36]

11.34 We recommend:

53. (a) A person should be entitled to be compensated by the Keeper for loss suffered in consequence of:

(i) an inaccuracy attributable to the Keeper in the making up, maintenance or operation of the Register of Assignations, or in an attempted correction of the register,

(ii) the issue of a statement or notification which is incorrect, or

(iii) the issue of an extract which is not a true extract.

(b) But the Keeper should have no statutory liability:

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[31] Compare LR(S)A 2012 s 106(1)(a) and (b).
[32] LR(S)A 2012 s 106(2)(a).
[33] LR(S)A 2012 s 106(2)(b).
[34] See *Allan v Barclay* (1864) 2 M 873, J M Thomson, *Delictual Liability* (5th edn, 2014) para 16.2 and *Simmons v British Steel Plc* 2004 SC (HL) 94 per Lord Rodger of Earlsferry at paras 59–67. We are grateful to Professor Elspeth Reid for her assistance here.
[35] See eg NZ PPSA s 176(1).
[36] LR(S)A 2012 s 106(2)(c). See Scottish Law Commission, Report on Land Registration (Scot Law Com No 222, 2010) para 22.58.

(i) in so far as the person's loss could have been avoided had the person taken measures which it would have been reasonable for the person to take,

(ii) in so far as the person's loss is not reasonably foreseeable, or

(iii) for non-patrimonial loss.

(Draft Bill, s 37)

Liability of certain other persons

11.35 We think that there should be two circumstances where others should have statutory liability for loss, but we think that this should be fault-based rather than strict. In this regard we have been influenced by section 111 of the Land Registration etc. (Scotland) Act 2012.[37] It requires, among other things, that persons applying for registration must take reasonable care to ensure that the Keeper does not inadvertently make the register inaccurate as a result of the application. For example, a forged deed should not be sent for registration.

11.36 The first circumstance of liability is in relation to someone who is responsible for the application which led to an erroneous entry which causes another party loss.[38] Example 1. Alice, a sole trader, assigns her invoices to a bank. But in the application for registration, the bank names Alison, another sole trader, as the assignor rather than Alice. This prevents Alison from assigning her invoices until the matter is sorted out. The bank should be liable to Alison for loss suffered.

11.37 Secondly, we consider that there should be liability in relation to the information duty provisions[39] for either (a) failure to respond to a request for information or (b) the supply of incorrect information.

11.38 Example 2. X Ltd, a multi-trades company, grants an assignation to the Y Bank of future invoices specified in schedules to be sent from X Ltd to the bank. X Ltd and the bank subsequently agree that for the most part only invoices for plumbing work will be assigned. A few months later X Ltd enters into negotiations with the Z Bank about assigning certain invoices for electrical work. The Z Bank searches the RoA and discovers the assignation. X Ltd advises that the arrangement is only for plumbing invoices. With X Ltd's permission, the Z Bank is entitled to have the Y Bank confirm this. The Y Bank, however, supplies wrong information and states that certain electrical invoices have been assigned to it when these have not. This means that X Ltd is prevented from assigning the invoices to the Z Bank. The Y Bank should be liable to X Ltd for loss suffered as a result.

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[37] See Reid and Gretton, *Land Registration* paras 15.2–15.5.

[38] See in this regard the Belgian Pledge Act of 11 July 2013 art 35 (which provides for art 29 of the new Book III title XVII of the Civil Code) and the DCFR IX.–3:306(e).

[39] See paras 11.2–11.14 above. We note that under the Security Interests (Jersey) Law 2012 art 85(6) failure to comply with an information request is a criminal offence. We do not follow this approach.

11.39 Example 3. Same as example 2. But the Y Bank simply ignores the information request. This effectively prevents X Ltd from assigning invoices to the Z Bank. The Y Bank should be liable to X Ltd for loss suffered as a result.

11.40 Example 4. Same as example 2. But X Ltd has in fact assigned electrical invoices and forgotten about this or is fraudulent. The Z Bank makes the information request to the Y Bank, which this time says wrongly that the electrical invoices have not been assigned. The Z Bank then takes an assignation of these invoices, which of course is ineffective as they have already been assigned to the Y Bank. The Y Bank should be liable to the Z Bank for loss suffered as a result.

11.41 As with the Keeper's liability, we think that liability here should be subject to the duty of the party claiming compensation to mitigate loss. There also should be no liability for loss that is not reasonably foreseeable or for non-patrimonial loss.

11.42 We recommend:

54. (a) Where a person suffers loss in consequence of:

(i) an inaccuracy in an entry in the Register of Assignations (which is not caused by the Keeper), the person should be entitled to be compensated for that loss by the person who made the application which gave rise to that entry if, in making it, that person failed to take reasonable care, or

(ii) a failure to respond to a request for information under the information duty provisions, or the provision of information in which there is an inaccuracy, the person is entitled to be compensated for that loss by the person who failed to supply the information if that failure was without reasonable cause or if, in supplying it, that person failed to take reasonable care.

(b) But there should be no liability:

(i) in so far as the person's loss could have been avoided had the person taken measures which it would have been reasonable for the person to take,

(ii) in so far as the loss is not reasonably foreseeable, or

(iii) for non-patrimonial loss.

(Draft Bill, s 38)

RoA Rules

11.43 While the main aspects of the RoA should be set out in primary legislation, there requires to be more flexibility on other aspects. Here secondary legislation is more

appropriate. This model can be found both in relation to the Land Register in Scotland,[40] as well as under the PPSAs.[41]

11.44 We consider therefore that the Scottish Ministers should have the power to make secondary legislation in relation to the RoA. These would be known as "RoA Rules". Below, we set out a formal recommendation as to matters on which RoA Rules should be capable of being made. Many of these are self-explanatory, but a few deserve comment.

11.45 We think that RoA Rules should be able to specify the degree of precision with which time is to be recorded in the register and thus displayed in the relevant entry. Earlier, we recommended automated electronic registration,[42] so it may be sensible to record the time to perhaps the nearest second rather than fraction of a second.

11.46 It should also be possible for RoA Rules to allow certain information in the assignation document, as well as any signatures, to be redacted in the interests of confidentiality and fraud prevention. This is similarly possible when documents are registered in the Companies Register.[43] We think also that it should be possible for certain information that is registered not to be visible to persons searching the register or to appear in extracts. We have in mind particularly dates of birth, where one possibility might be to withhold the day, as is done for director's details in the Companies Register. Another would be that while a name and date of birth search would take the searcher to any relevant entries the date of birth would not actually be displayed.[44]

11.47 RoA Rules could also set out when the register is open for registrations and searching. The PPSA registers are typically open 24 hours a day and 365 days a year, except for scheduled downtime.

11.48 Before making RoA Rules we think that the Scottish Ministers should be required to consult the Keeper.[45]

11.49 We recommend:

55. The Scottish Ministers should, following consultation with the Keeper, have the power to make rules (to be known as "RoA Rules")

(a) as to the making up and keeping of the register,

(b) as to procedure in relation to applications:

(i) for registration, or

(ii) for corrections,

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[40] See the LR(S)A 2012 s 115 and the Land Register Rules etc. (Scotland) Regulations 2014 (SSI 2014/150).
[41] See eg NZ PPSA 1999 and the Personal Property Securities Regulations 2001.
[42] See paras 6.40–6.45 above.
[43] Companies Act 2006 s 859G.
[44] See para 7.9 above.
[45] Cf LR(S)A 2012 s 115(2).

(c) as to the identification, in any such application of any person or claim, including:

(i) how the proper form of a person's name is to be determined, and

(ii) where the person bears a number (whether of numerals or of letters and numerals) unique to the person, whether that number must (or may) be used in identifying the person,

(d) as to the degree of precision with which time is to be recorded in the register,

(e) as to the manner in which an inaccuracy in the assignations record may be brought to the attention of the Keeper,

(f) as to information which, though contained in an assignation document, need not be included in a copy of that document submitted with an application for registration,

(g) as to whether a signature contained in an assignation document need be included in a copy of that document so submitted,

(h) as to searches in the register,

(i) as to information which, though contained in the register, is not to be:

(i) available to persons searching it, or

(ii) included in any extract issued by the Keeper,

(j) prescribing the configuration, formatting and content of:

(i) applications,

(ii) notices,

(iii) documents,

(iv) data,

(v) statements, and

(vi) requests,

to be used in relation to the register,

(k) as to when the register is open for:

(i) registration, and

(ii) searches,

(l) requiring there to be entered in the assignations record or the archive record such information as may be specified in the rules, or

(m) regarding other matters in relation to registration, being matters for which the Scottish Ministers consider it necessary or expedient to give full effect to the purposes of the draft Bill.

(Draft Bill, s 40)

Chapter 12 Assignation: debtor protection

General

12.1 In this chapter we consider what rules there should be to prevent a debtor being prejudiced by an assignation.

Debtors who perform in good faith to the assignor

12.2 In legal systems or international instruments where intimation is not required to complete an assignation, there are rules to protect debtors who perform to the assignor in good faith.[1] Thus say Albert owes Ben £1,000. Ben assigns his right to payment to Caroline. Albert, being unaware of the assignation, pays Ben. Albert is discharged of his debt. Under Scottish law, however, intimation to Albert is currently necessary to complete the assignation. Albert, on receiving intimation of the assignation to Caroline, would not be in good faith by paying to Ben.

12.3 There is therefore little authority on protection of good faith debtors in Scotland, but the doctrine is recognised.[2] Dr Ross Anderson notes: "The most common example will be postal intimation to the debtor. If the debtor pays the [assignor] in good faith because he never received the intimation before payment, he has a defence of good faith payment."[3] This reflects the difference which we highlighted earlier between the purpose of intimation of determining priority and the purpose of notifying the debtor.[4] Under our recommendations it becomes more likely that a debtor does not know of an assignation because assignations may be completed without intimation by registration in the Register of Assignations.[5]

12.4 We consider that where there has been an assignation of a claim, the debtor who performs in good faith to the person last known to the debtor to be the holder of the claim should be discharged.[6] To assist with the explanation we use the example above. Albert owes Ben £1,000. Ben is the person last known by Albert to be the holder of the claim. (If, however, Ben had assigned the claim to Zoe and Zoe had intimated to Albert, then Zoe would become the person last known to Albert to be the holder). Ben assigns the claim to Caroline. Caroline registers the assignation in the RoA but does not intimate to Albert.

12.5 Albert should be discharged if he pays the £1,000 to Ben in good faith (having had no intimation from Caroline), that is to say makes performance to the person last known to Albert to hold the claim. Good faith performance to the assignor should be interpreted broadly and be taken to include performing to a third party at the direction of the assignor.

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[1] For example, see the German Civil Code art 407(1). See also DCFR III.–5:119. In English law a similar result is achieved by means of the rule in *Dearle v Hall* (1828) 3 Russ 1. See para 5.65 above.
[2] Stair 1.18.3 and 4.40.33; *Hume v Hume* (1632) Mor 848. See generally Anderson, *Assignation* paras 7-01 to 7-10. See also P Nienaber and G Gretton, "Assignation/Cession" in R Zimmermann, D Visser and K Reid (eds), *Mixed Legal Systems in Comparative Perspective* (2004) 787 at 799–801.
[3] Anderson, *Assignation* para 7-10.
[4] See paras 5.26–5.28 above.
[5] See paras 5.1–5.22 above.
[6] Cf DCFR III.–5:119.

For example, Albert should be discharged if in good faith he pays the £1,000 to Deborah after having been directed by Ben to pay Deborah. As Albert believes Ben to be the holder of the claim he should be discharged where he has simply followed Ben's instructions. Similarly, Albert should be discharged if in good faith he pays the £1,000 to Ellie after Ben informing Albert that he has assigned the claim to Ellie. In all these cases if Albert only pays £500 of the £1,000 or any other part of the claim he should only be discharged to that extent.

12.6 We consider it unreasonable to expect debtors to check the register. This would involve time and cost. Therefore the fact that the assignation document has been registered should not of itself mean that a debtor is in bad faith as regards the assignation.[7] Similarly, the provisions which we recommend elsewhere,[8] which deem that notice is to be received after certain periods should not impact on Albert's good faith.

12.7 We think that the same rules should apply where Albert is a co-debtor and performs in good faith. Imagine that Albert and Alice are co-debtors to Ben for the debt of £1,000 and Albert pays Ben the £1,000 in good faith, being unaware of the assignation to Caroline. The result is that Albert and Alice, together being the debtor, should be discharged, but Albert would have a right of relief against Alice for £500 (subject to any contrary agreement between them) because they were co-debtors.[9]

12.8 An alternative approach would be to discharge a debtor (including a co-debtor) who makes performance to the assignor until such time as the debtor actually receives intimation of the assignation. It would not matter that the debtor was aware of the assignation by other means. This is the approach taken, for example, by the UNCITRAL Convention on the Assignment of Receivables in International Trade[10] and the UNCITRAL Model Law on Secured Transactions.[11] There is also some authority for it in our law, but ultimately the position is uncertain.[12] The attraction of this alternative approach is that it is simpler and more certain than one dependent on good faith.[13] On the other hand, it seems less fair that a debtor in full knowledge of an assignation can choose to ignore this because formal written notification has not been received. We consider that the certainty issue can be assisted by following the approach of German law,[14] so that the onus is on the assignee to show that the debtor is not in good faith. Thus Caroline would need to convince the court that Albert knew about the assignation, because, for example, she did intimate to him and she has evidence that he received the intimation.

12.9 We therefore hold to an approach based on good faith and recommend:

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[7] If, however, a debtor and creditor agree that the debtor should search the register against the creditor before making payment to check if an assignation has been registered, a failure to do so may mean that the debtor is regarded as being in bad faith.

[8] See paras 5.52–5.54 above.

[9] Bell, *Principles* § 62; W A Wilson, *The Scottish Law of Debt* (2nd edn, 1991) para 28.2.

[10] UNCITRAL Convention on the Assignment of Receivables in International Trade art 17.

[11] UNCITRAL Model Law on Secured Transactions art 61.

[12] See Anderson, *Assignation* para 6-25 fn 71.

[13] A point made to us by Professor Hugh Beale and Professor Louise Gullifer in their response to our draft Bill consultation of July 2017.

[14] German Civil Code art 407(1). But if intimation has been received by the debtor, it is then for the debtor to demonstrate good faith. See H Prütting, G Wegen and G Weinreich (eds), *BGB: Kommentar* (11th edn, 2016) § 407, Rn 7 and 10. We are grateful to Dr Ross Anderson for this reference.

56. (a) Where after a claim has been transferred by assignation there is performance by the debtor or any co-debtor to the assignor and that performance is in good faith, the debtor should be discharged to the extent of the performance.

(b) The fact only that an assignation document has been registered or that a notice of an assignation has been deemed to have been received, should not of itself mean that a debtor, or any co-debtor, is to be regarded as having performed other than in good faith.

(c) In any dispute as to whether performance was in good faith the burden of proof should lie on the party asserting that performance was other than in good faith.

(Draft Bill, ss 11 and 120)

Successive assignations

12.10 There is a second situation where we consider that a good faith debtor should be protected,[15] particularly in the light of our recommendation that an assignation of a claim could be completed by registration instead of intimation. It is best explained by an example. Lisa owes Kelly £5,000. Kelly assigns her claim against Lisa to Mhairi. Mhairi registers the assignation in the RoA. The claim is thus transferred to Mhairi, but there is no intimation to Lisa. Kelly then fraudulently assigns the same claim again to Nils. Nils intimates to Lisa. Lisa pays Nils in good faith. Here we consider that Lisa should be discharged.[16] Under English law, Lisa would also be discharged, but on a different basis, namely that Nils' intimation trumps the transfer to Mhairi, because Mhairi did not notify.[17] The rule which we recommend is merely a rule of debtor protection. The transfer to Mhairi would remain effective and she would have the right to recover the money from Nils.[18] He could then pursue Kelly for breach of warrandice on the basis that she did not have title to the claim when she assigned it to him.[19]

12.11 We consider that this rule of debtor protection should be similar to the general rule outlined above in that: (a) discharge should only be to the extent of the performance; (b) the debtor should not be regarded as not being in good faith merely because the assignation document has been registered or notice of the assignation has been deemed to have been received; and (c) it should be for a party asserting that the debtor is not in good faith to prove this.

12.12 We recommend:

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[15] See Nienaber and Gretton, "Assignation/Cession" at 800.
[16] Cf DCFR III.–5:119(3) and UNCITRAL Convention on the Assignment of Receivables in International Trade art 17(4).
[17] *Dearle v Hall* (1828) 3 Russ 1. See para 5.68 above.
[18] See Stair 4.40.33; Scottish Law Commission, Discussion Paper on Recovery of Benefits Conferred Under Error of Law (Scot Law Com DP No 95, 1993), vol 1, para 3.59. Similarly, for German law, see the German Civil Code art 816(2).
[19] On warrandice, see further paras 13.36–13.43 below.

57. (a) Where a claim (or one and the same part of a claim) has been assigned successively, the debtor should be discharged to the extent that the debtor (or any co-debtor) performs in good faith to the first assignee from whom intimation is received.

(b) The fact only that an assignation document has been registered or that a notice of an assignation has been deemed to have been received, should not of itself mean that a debtor, or any co-debtor, is to be regarded as having performed other than in good faith.

(c) In any dispute as to whether performance was in good faith the burden of proof should lie on the party asserting that performance was other than in good faith.

(Draft Bill, ss 12 and 120)

Performance in good faith where claim assigned is of a prescribed type

12.13 Earlier we recommended that the Scottish Ministers should have power to prescribe certain types of claim where an assignation requires to be completed by registration in the RoA and intimation does not effect transfer.[20] Imagine that certain types of trade invoice are prescribed. Jean is the customer (debtor) in respect of an invoice of the prescribed type. She receives intimation from a bank that the invoice has been assigned to it and she should make payment to it. The invoice has indeed been assigned to the bank but the bank fails to register the assignation in the RoA. Here we consider that Jean should be discharged to the extent that she pays the bank,[21] provided that she is in good faith.

12.14 Typically, Jean would be in good faith. For her not to be in good faith, we consider that she would have to *know* that (a) the assignation has not been registered (perhaps because the assignee has informed her of this) and (b) that the assignation of such an invoice requires registration for transfer (perhaps because she is a lawyer).

12.15 We recommend:

58. (a) Where a claim is of a type that has been prescribed as transferable only by registration and an assignation of that claim is not registered, but intimation of it is made to the debtor or a co-debtor, the debtor should be discharged to the extent that performance is made in good faith to the assignee.

[20] See paras 5.16–5.20 above.

[21] We think that the same result would be reached under a "priority" registration system such as that being proposed by the Financial Law Committee of the City of London Law Society and the Secured Transactions Law Reform Project for England and Wales. Under such a system if there is no registration the assignment will nevertheless be effective as between the assignor and assignee, so a debtor paying the assignee would be discharged.

(b) A debtor or co-debtor who knows that the assignation has not been registered and that transfer of the claim requires such registration should not be taken to perform in good faith.

(Draft Bill, s 13)

Wider good faith protection?

12.16 There is some authority supporting a general principle that debtors who perform in good faith should be discharged where they perform to the wrong person.[22] Take the following situation. Albert owes Ben £1,000. Crispin draws up an assignation document by Ben in his (Crispin's) favour and forges Ben's signature on it. Crispin intimates the "assignation" to Albert. Albert then pays Crispin in good faith. Crispin disappears. Should Albert be discharged? Unlike the situations in respect of which we have made recommendations above, there has not been an assignation by the holder of the claim. It is a difficult question of policy as to whether the debtor (Albert) should be protected over the holder (Ben). Both are innocent. Under the information duty provisions which we recommend below, a debtor in doubt as to whether there has been a valid assignation should be entitled to withhold performance until provided with reliable evidence of that assignation. This may assist, but we accept that a debtor might regard what later transpired to be a forgery as such evidence. A general rule protecting debtors who perform in good faith to the wrong person clearly could apply in situations where there was no assignation valid or otherwise and therefore we do not recommend express provision on the matter here.[23] It would of course be open to the courts to develop such a rule from the authority that already exists.

Debtor protection: information duties

12.17 Under the current law the debtor is protected by the assignation requiring intimation to effect it. Other than in the case of the intimation not actually reaching the debtor, by say going missing in transit, the debtor knows that there has been an assignation because of the requirement of intimation. Further, the Transmission of Moveable Property (Scotland) Act 1862 requires that the debtor is supplied with a copy of the assignation. Thus while the assignee who intimates may well be a stranger to the debtor, the debtor can see the assignation and the assignor's signature on it.

12.18 We saw earlier, however, that the requirement to send a copy of the assignation may be impractical.[24] It is also unclear following the decision of the Inner House in *Christie Owen and Davies plc v Campbell*[25] that there must be compliance with the 1862 Act.[26] Under our recommendations neither intimation nor supplying a copy of the assignation would be mandatory. This therefore brings the need for statutory information duties to the debtor,

[22] Stair 1.18.3 and 4.40.33; Anderson, *Assignation* para 7-02. See also the submission of defender in *Promontoria (Ram) Ltd v Moore* [2017] CSOH 88 at para 21.
[23] We note that the DCFR III.–5:119 (performance to person who is not the creditor) is also a limited provision.
[24] See para 5.46 above.
[25] [2009] CSIH 26; 2009 SC 436.
[26] See para 5.31 above.

which are a familiar feature of legal systems and international instruments where intimation is not a requirement.[27]

12.19 Under EU law it is a requirement that where a right against a consumer under a credit agreement is assigned "the consumer shall be informed of the assignment . . . except where the original creditor, by agreement with the assignee, continues to service the credit vis-à-vis the consumer."[28] This requirement does not add anything to current Scottish law because intimation is required in every case anyway, regardless of whether the debtor is a consumer or not. But under our recommendations, where intimation is no longer essential, it would have to be complied with in consumer credit agreement cases.

12.20 In the Discussion Paper we addressed the issue that intimation sent to the debtor could be in small print or otherwise in such a form that may not bring home to the debtor what it is. The problem is worse if the document is a large one. The provisions dealing with the assignation might be tucked away on page 93 of a 120 page document. The debtor should hardly be expected to search for them. We consider that in such a case the debtor should be protected by our earlier recommendations on good faith performance.[29] It is unreasonable for the debtor to have to read a 120 page document to be informed that the claim has been assigned. An intimation of an assignation should be succinct and clear. This is why we have recommended a model form.[30]

12.21 On the wider issue of information duties, we asked consultees when there should be such duties on the assignee and, if so, what they should be, and what should be the consequences of failure to perform them. We received a range of views from consultees. Aberdeen Law School argued that "it does seem sensible to force the assignee to at least prove an assignation has taken place." The Judges of the Court of Session said that "whatever the detail of any information duties upon the assignee, they should be sufficient to ensure that prima facie proof of the assignation is provided." Professor Eric Dirix believed that "the best rule is that if the notification is made solely by the assignee, the debtor has the right to request some proof of the assignment and is entitled in the meantime to withhold payment." David Cabrelli supported reform based on the DCFR. We have indeed found the DCFR rules[31] very helpful in formulating policy on information duties.

12.22 First, we consider that where intimation is made by the assignee (rather than the assignor) the debtor should be entitled to request from the assignee sufficient evidence of the assignation. This right would apply where the debtor has been sent a notice of the assignation. If, in contrast, intimation was made judicially, any question as to the validity of the assignation could be raised within the relevant proceedings. "Sufficient evidence"[32] should include the written confirmation of the assignor that there has been an assignation. Another way of providing evidence would be to supply a copy of the assignation but it may be that the parties do not want to do this for reasons of confidentiality.

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[27] For example under the German Civil Code art 410, the UNCITRAL Convention on the Assignment of Receivables in International Trade art 17(7) and the DCFR III.–5:120.
[28] Directive 2008/48/EC, Art 17(2), originally transposed into UK law by the Consumer Credit Act 1974 s 82A. See now the Consumer Credit Instrument 2014 (FCA 2014/11) rule 6.5.
[29] See paras 12.2–12.8 above.
[30] See para 5.45 above.
[31] DCFR III.–5:120.
[32] The term used in the DCFR is "reliable evidence" but "sufficient" is more familiar in Scotland in the context of proof.

12.23 Secondly, where there has been no intimation received but the debtor has reasonable grounds to believe that there has been an assignation (for example, they have private information in relation to this), the debtor should be entitled to written confirmation from the (supposed) assignor that the claim has been assigned or not assigned. Where the claim has been assigned the debtor should be given the name and address of the assignee (unless performance is still to be to the assignor, in which case the confirmation should include a note to that effect.)

12.24 There requires also to be a sanction where there is no compliance with the information duties. The approach of the DCFR is that the debtor can withhold performance until there is such compliance.[33] In contrast the UNCITRAL Convention on the Assignment of Receivables in International Trade permits the debtor to perform to the original holder of the claim until there is compliance.[34] On balance we think the DCFR approach better. The debtor should simply be entitled to withhold performance, rather than be entitled to perform to a party who may no longer in fact hold the claim.

12.25 Where there are co-debtors, we think that the rights to information should be exercisable by the co-debtors acting together rather than an individual co-debtor acting alone because it is in the interests of all the co-debtors that the true position is ascertained.

12.26 We recommend:

59. (a) A debtor to whom intimation of an assignation has been made by an assignee should be entitled to request from the assignee sufficient evidence of the assignation.

(b) "Sufficient evidence" should include the written confirmation of an assignor that an assignation to which that assignor is party has taken place.

(c) A debtor who has reasonable grounds to believe that a claim has been assigned should be entitled to ask the supposed assignor whether there has been an assignation.

(d) The supposed assignor should have to confirm in writing whether the claim has been assigned.

(e) Until the debtor receives the evidence or confirmation, the debtor should be entitled to withhold performance.

(Draft Bill, s 15)

[33] DCFR III.–5:120(4).
[34] UNCITRAL Convention on the Assignment of Receivables in International Trade art 17(7).

The *assignatus utitur jure auctoris* rule

General

12.27 This rule – often shortened to the *assignatus utitur* rule - is a longstanding part of the law of assignation in this country and others.[35] Its effect is that defences which the debtor can plead against the assignor can also be pled against the assignee. In other words, the debtor should not be prejudiced by the assignation.

12.28 The example which we gave in the Discussion Paper was as follows. Cosmo sells oats to Duncan for £10,000. The sale is on credit, and Cosmo assigns the invoice to Alison. The oats as delivered are of a quality that Duncan says is disconform to contract. If Duncan had the right to refuse to pay anything to Cosmo, he also has that right against Alison. If he had the right against Cosmo to pay a reduced sum, he also has that right against Alison. The fact that the assignee will, in the typical case at least, have taken the assignation in good faith is irrelevant.[36] Thus the rights of an account debtor are unimpaired by an assignation.

12.29 The rule also applies in relation to rights of compensation (set-off) of the debtor. For example, Gwyneth owes Henry £1,000 but Henry owes Gwyneth £250.[37] Gwyneth would be entitled to plead the defence known as compensation and set-off the £250, so that she only pays Henry £750. Imagine that Henry assigns the £1,000 claim against Gwyneth to Isabel. Gwyneth is still entitled to exercise her right of compensation and only pay Isabel £750. (Provided that the claim for £250 arose before the £1,000 claim was transferred).

Reform

12.30 In the Discussion Paper,[38] we took the view that the *assignatus utitur* rule was a sound one. The only issue we highlighted was whether a contract might be subject to special rules of interpretation after an assignation, in favour of a good faith assignee. This was an issue mentioned in our 2011 Discussion Paper on Interpretation of Contracts.[39] Our provisional view was that no exception should be made to the *assignatus utitur* rule. We inclined to think that the law in this area did not stand in need of legislative intervention. But we sought the views of consultees on whether any reform was needed, and also on whether it might be of value if the rule were given a statutory form.

12.31 All the consultees who responded on this matter considered that no legislation was required. When, however, we came to consider the issue as we worked on the draft Bill appended to this Report we came to the view that it would be necessary to make express provision in relation to compensation (set-off). Under the current law the cut-off time in respect of which this can be pled is the time of intimation, that is to say the time that the

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[35] See, for example, Stair 2.1.20 and the French Civil Code art 1216(2).
[36] Cases on the *assignatus utitur jure auctoris* doctrine are numerous. See eg *Johnstone-Beattie v Dalziel* (1868) 6 M 333; *Scottish Widows Fund v Buist* (1877) 4 R 1076; *Train v Clapperton* 1907 SC 517 aff'd 1908 SC (HL) 26.
[37] This example is given also at para 3.13 above.
[38] Discussion Paper, para 14.73.
[39] Scottish Law Commission, Review of Contract Law: Discussion Paper on Interpretation of Contract (Scot Law Com DP No 147, 2011) paras 7.32 and 7.35.

assignation is completed.[40] Thus the debtor can set-off claims owed by the assignor which arise prior to that time. Under our recommendations set out earlier[41] assignations would be able to be completed by registration in the RoA as well as by intimation. But in respect of compensation (including a right of contractual set-off where this the basis of that right is the contract which gave rise to the claim),[42] we think that the cut-off point should be when the debtor would no longer have been in good faith had the debtor performed to the assignor, notwithstanding that there has been earlier registration. The debtor cannot be expected to check the register. Normally the debtor would cease to be in good faith on receiving intimation of the assignation. Similarly, the provisions which we recommend elsewhere,[43] which provide that notice is deemed to be received after certain periods should not impact on the debtor's good faith.

12.32 The reason for using the debtor's state of knowledge to determine the cut-off point is that we consider that debtors should not be prejudiced by an assignation which they do not know about. It follow that the debtor should be able to plead compensation in respect of cross-claims against the assignor until intimation of the assignation is received. On the other hand it would not be fair to allow the debtor to make such a plea in respect of subsequently arising claims against the assignor as this would mean that the debtor would effectively have the power to reduce the value of the claim now held by the assignee.[44] One member of our advisory group[45] has expressed concern that a rule based on good faith is insufficiently certain. But our view is that an assignee has it within their power to achieve certainty by making sure that a clear intimation reaches the debtor.

12.33 Having concluded that provision is needed on this matter, we came to the view that there would be advantage in putting the general *assignatus utitur* rule into statutory form. This would see it being expressed in modern language as it is in international instruments,[46] rather than recourse having to be made to Latin. This would fulfil one of our duties, that is to make the law more accessible.[47]

12.34 We therefore recommend:

60. (a) The *assignatus utitur jure auctoris* rule should be put into statutory form, that is to say the debtor (or any co-debtor) should be able to assert against the assignee all defences that the debtor could assert against the assignor.

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[40] In English law equitable set-off (where the claim and cross-claim are so closely related that it would be regarded as unconscionable to enforce the claim without taking the cross-claim into account) can be asserted against an assignor even after notice (intimation). See *Bibby Factors Northwest Ltd v HFD Ltd* [2015] EWCA Civ 1908 and Gullifer (ed), *Goode and Gullifer on Legal Problems of Credit and Security* para 7-73. Scottish law appears otherwise. See Anderson, *Assignation* para 8-53.

[41] See paras 5.1–5.22 above.

[42] See Anderson, *Assignation* para 8-60.

[43] See paras 5.52–5.55 above.

[44] See Gullifer (ed), *Goode and Gullifer on Legal Problems of Credit and Security* para 7-73.

[45] Dr Hamish Patrick.

[46] For example, UNIDROIT Factoring Convention art 9; UNCITRAL Assignment Convention art 18; DCFR III.–5:116 and the UNCITRAL Model Law on Secured Transactions art 64. And see also the Code civil art 1324 (France).

[47] Under the Law Commissions Act 1965 s 3(1) we are required to work towards the "simplification and modernisation of the law".

(b) The debtor (or any co-debtor) should be able to assert against the assignee any right of compensation (including a right of contractual set-off where the basis of that right is the contract which gave rise to the claim) available to the debtor against the assignor up to the time when the debtor would no longer have been in good faith had the debtor performed to the assignor.

(c) The fact only that an assignation document has been registered or that a notice of an assignation has been deemed to have been received, should not of itself mean that a debtor, or any co-debtor, is to be regarded as having performed other than in good faith.

(Draft Bill, s 14(1) to (3) & (5))

Waiver-of-defence clauses

12.35 Where the debtor renounces the right to plead against an assignee substantive defences which could have been pled against the assignor this is known as a "waiver-of-defence" clause.[48] The effect of this is to make the claim more marketable. Some legal systems recognise the validity of such a clause.[49] Though such clauses are quite often used in Scotland, their effect seems to be untested in the courts. But as far as the common law is concerned, there would seem to be no reason why they should not be valid.[50]

12.36 We asked consultees whether the law here should be clarified. We took the view that if waiver-of-defence clauses are to be given statutory force then presumably they should be of no effect against consumers. In general, consultees who responded to this question favoured such clauses being enforceable in a business but not a consumer context. Professor Eric Dirix said that in civil law systems the matter of defences and exceptions is left to the principle of contractual freedom, except for certain limitations based on consumer protection. Several consultees pointed out that consumers were already protected by legislation here. Reference was made to the Unfair Contract Terms Act 1977 and the Unfair Terms in Consumer Contract Regulations 1999.[51] These have now been replaced in the consumer context by the Consumer Rights Act 2015.[52] We share the view of these consultees that the matter should be left to this legislation.

12.37 There is then the matter of whether provision should be made to declare such clauses otherwise effective. A number of consultees pointed out that this seems essentially

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[48] The debtor must agree to waive the defence. Thus a waiver-of-defence clause in a notice intimating an assignation will only be effective where the debtor signs and returns a copy of the notice to the assignee agreeing to its terms.

[49] For example UCC § 9–403; Saskatchewan PPSA 1993 s 41(2); Ontario PPSA 1990 s 14; New Zealand PPSA 1999 s 102(2); Australian PPSA 2009 s 80(2).

[50] But they may be struck at by consumer protection legislation as we note in the next paragraph. The position is similar in other jurisdictions. See eg Gedye, Cuming and Wood*, Personal Property Securities in New* Zealand 370.

[51] SI 1999/2083 implementing Directive 93/12/EEC. See in this regard *Coca-Cola Financial Corporation v Finsat International Ltd* [1998] QB 43; *Axa Sun Life Services Plc v Campbell Martin Ltd* [2011] EWCA Civ 133 at para [75].

[52] See Part 2 of that Act. Under section 62(1) an unfair term of a consumer contract is not binding on the consumer. And see in particular Sch 2, para 2.

a matter of freedom of contract. In the Discussion Paper[53] we noted that the statement of the *assignatus utitur* rule in the DCFR[54] is in such unqualified terms that it is doubtful whether a waiver-of-defence clause would be regarded as valid. In contrast, other statutory models confirm that such a clause is valid. Since we have decided to recommend that the *assignatus utitur* rule be placed in statutory form we have concluded that the validity of waiver-of-defence clauses should also be confirmed.

12.38 We recommend:

61. (a) The debtor and the assignor should be able to agree that any defences which the debtor may assert against the assignor may not be asserted against an assignee.

(b) This should be without prejudice to any other enactment.

(Draft Bill, s 14(1) & (4))

[53] Discussion Paper, para 14.74.
[54] DCFR III.–5:116.

Chapter 13 Assignation: miscellaneous issues

Introduction

13.1 In this chapter we deal with the remaining issues relating to assignation covered in the Discussion Paper. These include anti-assignation clauses; mandates; transfer of entire contracts; accessory rights; assignations in security; and codification.

Anti-assignation clauses

13.2 Contracts may contain anti-assignation clauses.[1] The effect of such a clause is that if a party to the contract thereafter purports to assign, the assignation is ineffective. The common law is the same in both Scotland and England.[2] In other words, such a clause has effect not only as between the contracting parties themselves but also as against any purported assignee.[3]

13.3 Thus if Cosmo contracts to do construction work for Duncan, and the Cosmo/Duncan contract says that Cosmo is not to assign, and he nevertheless purports to assign the contract price to Abigail, she thereby acquires no right against Duncan. Such clauses are used for various reasons. One is convenience. It is administratively simpler for Duncan to know that he is to pay Cosmo, and not have to deal with the possibility that the claim has become payable to someone else. Another reason is that in some types of contract, assignation may give rise to potential difficulties. For example, a contract may contain an arbitration clause, and if there were to be an assignation, that might give rise to questions as to the position of the assignee in relation to the arbitration clause. Barring assignation means that such questions should not arise.

13.4 There is a strong tendency nowadays internationally for such clauses to take effect only as between the parties, so that breach merely amounts to a breach of contract, without making the assignation actually invalid.[4] The Law Commission for England and Wales has

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[1] These are also known as non-assignment clauses.

[2] See *James Scott Ltd v Apollo Engineering Ltd* 2000 SC 228 and *Linden Gardens Trust Ltd v Lenesta Sludge Disposal Ltd* [1994] 1 AC 85.

[3] Dutch law takes the same approach: see R G Anderson and J W A Biemans, "Reform of Assignation in Security: Lessons from the Netherlands" (2012) 16 EdinLR 24 at 47.

[4] See eg UCC § 9–406; Australian PPSA 2009 s 81; DCFR III.–5:109; UNCITRAL Convention on the Assignment of Receivables in International Trade art 9 and UNIDROIT Convention on International Factoring art 6. But cf G J Tolhurst and J W Carter, "Prohibitions on assignment: a choice to be made" 2014 Cambridge Law Journal 405. See also N O Akseli, "Contractual prohibitions on assignment of receivables: an English and UN perspective" 2009 JBL 650; R Goode, "Contractual Prohibitions against Assignment" [2009] LMCLQ 300; H Beale, L Gullifer and S Paterson, "Ban on Assignment Clauses: Views from the Coalface" 2015 Journal of International Banking and Financial Law 463; L Gullifer, "Should Clauses Prohibiting Assignment be Overridden by Statute?" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 319–336; N O Akseli, "The United Nations Convention on the Assignment of Receivables in International Trade and Small Businesses" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 465 at 473; H Beale, L Gullifer and S Paterson, "A case for interfering with freedom of contract? An empirically-informed study of bans on assignment" 2016 JBL 203 and N O Akseli, "Non-assignment Clauses and their Treatment under UNCITRAL's Secured Transactions Laws Instruments in S V Bazinas and N

recommended that English law should take the same approach[5] and this is now the position in Jersey.[6] Sometimes statutory provisions in relation to these clauses apply generally,[7] whilst others are limited to trade receivables.[8]

13.5 The general rule for *real* rights such as ownership is that an agreement not to alienate has contractual effect between the parties but goes no further than that, so that it does not invalidate a transfer made in breach of the agreement.[9] Should that approach be followed for personal rights? The issue is, therefore, in reality not about freedom of contract but about the consequences of breach. Thus an anti-transfer clause should merely have the same effect in relation to the transfer of contract rights as it does for real rights. Hence a creditor who proposed to assign in breach of an anti-assignation clause could be interdicted, and if the assignation had already taken place, damages would be due if any loss could be shown to have followed from the breach. The difference would be that the transfer would be wrongful (but valid) rather than, as under the current law, invalid.

13.6 In the Discussion Paper, we said that we were not persuaded that a case exists to alter the law.[10] It had been suggested to us that altering the current law could upset carefully structured contracts. But to test opinions we asked whether, if a contract between X and Y contains an anti-assignation clause, and nevertheless there is a purported assignation by X of a right arising from the contract, the effect of the clause should be (as under the current law) that the assignation of that right is invalid, or that the only consequence should be that there has been a breach of contract by X. Secondly, we asked whether the rule should vary according to the type of case. For example, the rule might only apply to receivables but not to other claims. If that were to be the case, we asked which rule should apply to which type of case.

13.7 Most of the consultees who responded to this question did not favour reform of the law. Brodies noted that a breach of contract claim may be of limited value if the defender does not have funds to satisfy such a claim. The Law Society of Scotland said that it did "not believe that it would assist commerce to have a general rule overriding the parties' ability to agree provisions relating to assignability."

13.8 But Dr Ross Anderson said that there was no good answer to the questions. He pointed out that freedom of alienation and freedom of contract can be invoked to justify both validity and invalidity of an assignation in breach of an anti-assignation clause.[11] ABFA and the WS Society took the view that it would be helpful for legislation to clarify that a blanket ban on assignation of rights under a contract should not necessarily mean, unless the wording is explicit, that the right to receive payment could also not be assigned.

O Akseli (eds), *International and Comparative Secured Transactions Law: Essays in honour of Roderick A Macdonald* (2017) 77–93.

[5] Law Com Report No 296 para 4.40.

[6] Security Interests (Jersey) Law 2012 art 39(1).

[7] Such as DCFR III.–5:109.

[8] Such as those recommended by Law Com Report No 296.

[9] But in some types of case the "offside goals rule" applies with the result that the transfer is voidable (though not void). See Reid, *Property* paras 695–700.

[10] Discussion Paper, para 14.47.

[11] He referred to G Gilmore, *Security Interests in Personal Property* vol 1 (1965) 212-213. See also C Rudolf, *Einheitsrecht für internationale Forderungsabtretungen* (2006) 263.

13.9 Dr Hamish Patrick's position was that the current law should be maintained and that any exceptions should be a matter of policy in the area in question following specific consultation in that area to address a specific identified problem.

13.10 Since the publication of the Discussion Paper, there has been an important development.[12] Section 1 of the Small Business, Enterprise and Employment Act 2015 allows the Scottish Ministers[13] by regulations to make provision that anti-assignation clauses in relation to receivables in relevant contracts have no effect, or to have no effect in relation to certain persons that are prescribed.[14] A contract is a "relevant contract" if (a) it is a contract for goods, services or intangible assets (including intellectual property) which is not an excluded financial services contract, and (b) at least one of the parties has entered into it in connection with the carrying on of a business".[15] There is a long list of excluded financial services contracts in section 2 of the 2015 Act and further instances can be prescribed. The target of the legislation is trade receivables. At the time of writing the Scottish Ministers have not consulted on draft Regulations, but DBIS[16] has in England and Wales.[17]

13.11 We conclude that the general law on anti-assignation clauses should be left as it is, but that this should be subject to specific enactments such as the 2015 Act. We recommend:

> **62. (a) The ability of the holder of a claim to assign should be subject to any enactment, or any rule of law, by virtue of which a claim is not assignable.**
>
> **(b) Subject to any other enactment, an assignation of a claim should be ineffective in so far as the debtor and the holder of the claim agree, or the person whose unilateral undertaking gives rise to the claim states, that the claim is not to be assigned.**
>
> (Draft Bill, s 7)

Assignability: other issues

13.12 Aside from anti-assignation clauses, there were other issues in relation to the assignability of claims which we mentioned in the Discussion Paper.[18] One was where a contract confers powers on the creditor, such as a power to vary an interest rate. We thought that this might bar assignation, or possibly mean that the assignee cannot exercise that power. We also raised the issue of an arbitration clause in the original contract and the effect of that following assignation.[19] We asked consultees whether they thought that the law

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[12] See G Yeowart and R Parsons, *The Law of Financial Collateral* (2016) paras 24.62–24.93.
[13] And in England and Wales, and Northern Ireland, the Secretary of State. See Small Business, Enterprise and Employment Act 2015 s 1(6).
[14] 2015 Act s 1(1).
[15] 2015 Act s 1(3).
[16] Department for Business, Innovation and Skills. Now Department for Business, Energy and Industrial Strategy.
[17] See https://www.gov.uk/government/consultations/invoice-finance-nullifying-the-ban-on-invoice-assignment-contract-clauses. See also R Calnan, "Ban the Ban: Prohibiting Restrictions on the Assignment of Receivables" 2015 Journal of International Banking and Financial Law 136.
[18] Discussion Paper, para 14.59.
[19] See generally J C Landrove, *Assignment and Arbitration: A Comparative Study* (2009).

about assignability of contract terms conferring powers on the creditor, stood in need of reform and, if so, how.

13.13 Consultees who responded to this question generally did not favour reform. These included the Faculty of Advocates and the Law Society of Scotland. John MacLeod and Dr Hamish Patrick expressed the view that assignees would have the power to vary an interest rate if this was conferred on the assignor in the original contract. They considered that any restriction on this should be a matter for consumer protection law. We agree and consider that this would be most appropriately considered on a UK-wide basis, given that the subject matter of the Consumer Credit Act 1974 is a reserved matter.[20]

Mandates etc

13.14 Since assignation as such did not exist in Roman law, a functional equivalent gradually developed. If Gaius owed Julia money, she could "assign" to Claudia by granting her a mandate to collect from Gaius.[21] By late Roman law this had reached the point at which it was fairly close to a true assignation.

13.15 Scottish law appears to have developed the assignation in the mediaeval period.[22] The concept does not seem to have been borrowed from Roman law, and thus did not (contrary to what is often said) develop out of mandate. Scottish law therefore did not need to borrow from the less-developed Roman law on this topic. But the influence of Roman law was so strong that the Roman quasi-assignation came to influence Scottish law. Two results of this "assignation as mandate" idea are: (a) a mandate to collect, if granted for onerous consideration, takes effect as an assignation;[23] and (b) an assignee can sue in the name of the assignor.[24]

13.16 In the Discussion Paper we set out our view that these rules are not satisfactory.[25] We considered that if a creditor wishes to give a mandate to someone else to collect a debt, that this should be possible, without the arrangement being converted by force of law into an assignation. As for the doctrine that the assignee can sue in the assignor's name, we noted that while it is not important in practice, it still seems unsatisfactory. The effect of a successful action is that the debtor *is ordered to pay the wrong person*, that is a person who is not his creditor. For example, what if X assigns to Y, and Y then raises an action in X's name, and decree is pronounced, and X is now insolvent. Who gets the benefit of the decree: Y or X's creditors?

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[20] Scotland Act 1998 Sch 5 Part II Head C7. See paras 1.39–1.42 above.
[21] For the history see R Zimmermann, *The Law of Obligations: Roman Foundations of the Civilian Tradition* (1990) ch 13 and Anderson, *Assignation* ch 4.
[22] It seems likely that there was a strong French influence.
[23] *National Commercial Bank of Scotland Ltd v Millar's Tr* 1964 SLT (Notes) 57 at 59 per Lord Cameron.
[24] Anderson, *Assignation* paras 2-25 to 2-33. See also N R Whitty, "Mandates to Pay, Unjustified Enrichment and the Pandectist Deficit" in A J M Steven, R G Anderson and J MacLeod (eds), *Nothing as Practical as a Good Theory: Festschrift for George L Gretton* (2017) 136–149.
[25] Discussion Paper, paras 4.46–4.50 and 14.48–14.50.

13.17 Formerly assignations were chargeable to stamp duty, but mandates were not. Thus mandates were used to circumvent the tax. But this incentive to use mandates disappeared with the abolition of stamp duty on assignations.[26]

13.18 We asked consultees whether they agreed that (a) the rule that a mandate can operate as an assignation should be abrogated; and (b) the rule whereby an assignee can sue in the name of the assignor should be abrogated.

13.19 Most consultees who responded to these questions agreed. A minority argued that it may be difficult to distinguish an assignation document from a mandate document. We consider, however, that this concern can be addressed by documentation being made clear. Dr Ross Anderson raised an important issue, namely that a rule preventing assignees suing in the name of assignors would significantly affect reparation cases where insurers sue in the name of the injured party. In his view, subrogation is a type of assignation. We therefore consider that the rule should not apply in subrogation cases.

13.20 We recommend:

63. (a) The following rules of law should no longer have effect:

(i) any rule whereby a mandate may operate as an assignation of a claim;

(ii) any rule whereby an assignee of a claim may sue in the name of an assignor.

(b) But this should be without prejudice to the application of any enactment or rule of law as respects subrogation.

(Draft Bill, s 17(1)(a) & (c), and (2))

Policies of Assurance Act 1867

13.21 The Policies of Assurance Act 1867 provides for the assignment of insurance policies. It was passed to make it possible in England for life assurance policies to be assigned at law (and not merely equitably assigned, as formerly). In Scotland they had always been assignable. The intention was apparently that the Act was not intended to apply in Scotland,[27] but it has no express provision on the matter. As far as we can ascertain the Act has never been applied in any Scottish case. But some texts cite it as if it is in force here.[28]

[26] See Anderson, *Assignation* paras 3-18 and 5-41.

[27] Cf F A R Bennion, *Bennion on Statutory Interpretation* (6th edn, 2013) 316. The fact that the Transmission of Moveable Property (Scotland) Act 1862 expressly applies to policies of assurance of any assurance company or association in Scotland, irrespective of the place of residence of the policy holder, and was not amended by the 1867 Act also provides evidence that the 1867 Act was never intended to apply in Scotland. We are grateful to Dr Ross Anderson for drawing this to our attention.

[28] See, for example, Gloag and Irvine, *Law of Rights in Security* 530.

13.22 In the Discussion Paper,[29] we considered that it would make sense to amend the 1867 Act so as to confirm that it does not apply in Scotland. The consultees who responded on this issue either agreed or did not regard it as a material issue. We therefore hold to the view we expressed in the Discussion Paper, but because insurance law is reserved to the UK Parliament[30] we make no provision in our draft Bill on the matter.

13.23 We recommend:

64. The Policies of Assurance Act 1867 should be amended to confirm that it does not apply in Scotland.

Transfer of entire contracts

13.24 Some legal systems have rules on the consensual transfer of an entire contract. Thus a contract between D and E becomes a contract between D and F, with F succeeding to both the rights and the obligations of E, and E being discharged of any liabilities to D.[31] In the Discussion Paper,[32] we inclined to think that the issue was already adequately covered by the general law of contract, and that accordingly no legislative intervention was needed. But we sought the views of consultees. Consultees agreed.

13.25 We recommend:

65. There should be no statutory provision made in relation to the transfer of entire contracts.

Assignation and accessory security rights

13.26 Security rights are accessory to the claims that they secure. In principle, therefore, when a secured claim is assigned, the security should follow the claim.[33] This is part of a wider rule that the assignation carries all accessory rights and is familiar in other legal systems.[34] Thus Erskine writes: "Assignations, when properly perfected, carry to the assignee all rights which corroborate or strengthen the right conveyed."[35] Such rights include security over property as well as cautionary obligations (guarantees of third parties). But, as we noted in the Discussion Paper,[36] the law is not in a wholly satisfactory state.

13.27 To promote clarity and certainty, we thought that there might be a case for a general provision to the effect that, unless otherwise agreed, an assignation carries with it any security that exists for the assigned claim, and that if any further act is needed to vest the security in the assignee, the assignor will perform that act.[37] Thus, for example, if X owes

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[29] Discussion Paper, para 14.69.
[30] Scotland Act 1998 Sch 5 Part 2 Head A3.
[31] DCFR III.–5:302.
[32] Discussion Paper, para 14.76.
[33] On the difficulties arising where the claim and security right are held by different people, see *3D Garages Ltd v Prolatis Co Ltd* [2016] SC EDIN 70, 2016 GWD 34-617, discussed in K Swinton, "Three and four party heritable securities: now available in 3D!" 2017 SLG 60.
[34] See eg French Civil Code art 1321.
[35] Erskine 3.5.8. See also Stair 3.1.17; Anderson, *Assignation* para 2-01; Steven, *Pledge and Lien* para 4-18; and A J M Steven, "Accessoriness and Security over Land" (2009) 13 EdinLR 387 at 403–410.
[36] Discussion Paper, Chapter 5.
[37] This was the view taken by Lord Gifford in *McCutcheon v McWilliam* (1876) 3 R 565: "The conveyance of the debt is implied necessarily in conveying the subject of the security."

money to Y, secured by a standard security,[38] and Y assigns the claim to Z, without there being any assignation of the standard security, Z would have the right as against Y to have the security assigned.[39]

13.28 It would be possible to go further, and provide that an assignation of the secured claim automatically gives to the assignee a completed title to the security.[40] This is perhaps the most logical solution. But it would be a radical reform and would affect the law of standard securities. It would reduce the "publicity" value of registration as the register would not state the holder of the standard security.[41] We sought the views of consultees on this and also on the more general question of whether it should be provided that unless otherwise agreed, the assignation of a claim should carry with it a right to acquire any security that exists for the assigned claim, and that if any further act is needed to vest the security in the assignee, the assignor should perform that act.

13.29 Most consultees who responded to the general question agreed. But some law firm consultees were opposed, arguing that the transfer of the security should require to be dealt with expressly by the parties. A particular concern which these and some other consultees had was the situation where the secured obligation is more extensive than the security. Take the following example. Alice borrows £10,000 from Bertie. In return she grants him a standard security for all sums due to him. Such a security right, as the name suggests, will secure the entire indebtedness of the debtor to the secured creditor. One year later Alice borrows another £5,000 from Bertie under a separate loan contract. Bertie then assigns his claim to repayment under that contract to Cecilia. What is to happen to the security? Probably the law says that it is shared as between Bertie and Cecilia,[42] but this result is complex and normally in practice the parties would regulate this expressly.

13.30 We consider that a simple default rule should apply. The assignee should acquire, as a result of the assignation, the right to any security which relates to the claim assigned and is restricted to that claim. Thus in the case of the assignation of one of a number of claims secured by the security the right to the security would remain with the assignor. Of course, as a default rule the parties could make alternative provision. As a matter of policy we think that this should require to be made in the assignation document.

13.31 Again in the interests of simplicity, we think that the default rule should be that where a claim is assigned in part, the security should not pass to the assignee. Thus, for example, Donald owes Eric £10,000 secured by a standard security. Eric assigns £2,500 of his £10,000 claim against Eric to Fiona. The right to the standard security should remain with Eric, unless express provision to the contrary is made.

13.32 With some security rights it would be necessary for more to be done to vest the security in the assignee.[43] The alternative approach outlined above of the assignee

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[38] Or other right in security.
[39] It may be that this is already the law.
[40] See Anderson, *Assignation* para 2-13 to 2-14.
[41] For the position as regards statutory pledge, see paras 23.41–23.48 below.
[42] See Anderson, *Assignation* para 2-15 to 2-16. See also C G van der Merwe and E Dirix, "A Comparative Law Review of Covering Bonds and Mortgages Securing Fluctuating Debts" 1997 Stellenbosch Law Review 17 at 26–29.
[43] Note in this regard the Belgian Pledge Act of 11 July 2013 art 28 (which provides for art 23 of the new Book III title XVII of the Civil Code).

automatically obtaining a completed title in all cases would appear a step too far. Hence, for a claim secured by a possessory pledge, it would seem that the pledged property would have to be delivered to the assignee[44] and in the case of a standard security there would require to be an assignation of that security and registration of that assignation in the Land Register.

13.33 We recommend:

> **66. (a) Unless the assignor and assignee provide otherwise in the assignation document, where a claim is assigned in whole, the assignee should acquire, by virtue of the assignation, any security which relates to the claim assigned and is restricted to that claim.**
>
> **(b) The assignee should be required to perform any act requisite for the transfer of the security to the assignee as soon as reasonably practicable.**
>
> (Draft Bill, s 16)

13.34 A related issue is what should happen if there is a deed assigning the claim and the security, and this is registered in the relevant register, for example, an assignation of a standard security registered in the Land Register. At that stage there may have been no intimation to the debtor. If the law continues to be that assignation requires some external act to take effect, we asked whether it should be provided that the registration transfers the claim. For example, Doris owes money to Chris secured by standard security. Chris assigns the claim and the security to Audrey and this is registered in the Land Register on 1 June. Should the law be that the assignation of the claim is complete at the same time as the assignation of the security, that is on 1 June, even though there is no notification to Doris until later?[45] In more general terms, the question is whether the registration should transfer the claim notwithstanding that the general requirements of the law as to transfer of claims have not been met. Any such rule would of course require to be subject to protections for Doris in the event that she pays Chris in good faith, and so on. The reason for such a reform would be to prevent a split between the claim and the security.

13.35 There was little support from consultees for such a reform. Dr Ross Anderson and John MacLeod noted that it inverted the basic principle that the accessory (the security) follows the principal (the claim). The Law Society of Scotland thought that there could be difficulties caused by the transfer of the claim being dependent on the completion of conveyancing (although, earlier intimation would deal with this). Brodies raised issues with the assignation of all sums standard securities. In the light of the views of consultees we do not recommend this reform, but we may revisit the matter in our forthcoming project on heritable securities.

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[44] See Steven, *Pledge and Lien* paras 4-18 to 4-27. But compare Anderson, *Assignation* paras 2-05 to 2-06.
[45] It is possible that this might be the current law. But no-one can be certain.

Warrandice

13.36 When a claim is assigned, the law implies certain guarantees by the assignor to the assignee. This is known as "warrandice" and is a feature of the law as regards the transfer of all types of property.[46] The parties can exclude the implied guarantees or conversely agree on additional guarantees.

13.37 In the Discussion Paper we said that what the law implies in relation to the assignation of a claim is warrandice *debitum subesse*, that is to say that the assignor guarantees to the assignee the existence of the claim.[47] This means that if the assignee finds that the claim is barred, wholly or partially, by a plea of *assignatus utitur jure auctoris*[48] the assignor is in breach of warrandice and must compensate the assignee. We went on to say that the guarantee is only that the debtor is bound to perform, not that the debtor will actually make performance. We gave the example of the assignee being unable to obtain payment from the debtor because the debtor is insolvent. We did not ask consultees any questions in relation to warrandice in the Discussion Paper.

13.38 On reflection, following comments made to us by Professor Kenneth Reid, we consider that there would be advantage in placing the law here onto a statutory footing. The main reason for doing so is that the common law is unclear, as has been shown by Professor Reid[49] and also in more recent scholarship by Dr Chathuni Jayathilaka.[50] And in recommending a new statutory rule we consider that the common-law position that the parties are free to make contrary provision would be maintained. For example, in response to our draft Bill consultation, R3 noted that insolvency practitioners do not provide any form of warrandice. They would be able to maintain that position under our recommendations. In line with the common law too we think that a distinction requires to be made as regards assignations for value (typically where claims are sold) and assignations where there is no consideration (payment) made by the assignee.

13.39 For assignations for value and drawing on the admittedly unclear common law, we consider that the implied guarantee should be threefold. First, assignors would be taken to warrant that they are entitled to transfer the claim to the assignee, or in the case of the assignation of a future claim will become so entitled. This would require that they were the holder of the claim, or, in the case of a future claim, would become the holder. In addition, the claim would require to be assignable to the assignee. So if there were a ban on assignation resulting in transfer being debarred the assignor would be liable.[51] Secondly, there should be an implied guarantee that the debtor is bound to perform to the assignor in full. This means that the debtor should not have any defence such as that the claim is invalid, or be able to plead compensation (set-off) and only perform in part. Thirdly, assignors should be taken to warrant that they have done nothing in the past and will do nothing in the future to jeopardise the assignation, for example by granting an assignation of

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[46] See Reid, *Property* paras 701–800 and C Jayathilaka, *Sale and the Implied Warranty of Soundness* (forthcoming) paras 5-39 to 5-65.
[47] Discussion Paper, para 4.25.
[48] See paras 12.26–12.31 above.
[49] Reid, *Property* para 717.
[50] C Jayathilaka, "The Warrandices Implied in the Sale of a Claim to Payment" 2016 Juridical Review 105.
[51] See paras 13.2–13.11 above.

the same claim to another party. At common law, this is referred to as "fact and deed" warrandice.[52]

13.40 Where the assignation is not for value, assignors should be taken to warrant that they will do nothing in the future to prejudice the assignation. This is referred to by the common law as "simple warrandice".[53]

13.41 We think that the new statutory rule should make it clear as under the common law that there is no guarantee that the debtor will perform.[54] As mentioned earlier, the reason for non-performance will typically be insolvency.[55]

13.42 Finally, there is also doubt at common law whether warrandice is also implied in any contract (or unilateral undertaking) which precedes the assignation.[56] Normally of course this will be a contract of sale. In the case of transfer for no consideration there will probably not be any prior contract.

13.43 We recommend:

67. (a) In assigning a claim for value the assignor should be taken to warrant to the assignee that:

(i) the assignor is entitled to, or (in the case of a future claim) will be entitled to, transfer the claim to the assignee,

(ii) the debtor is obliged to perform in full to the assignor, and

(iii) the assignor has done nothing and will do nothing to prejudice the assignation.

(b) In assigning a claim other than for value the assignor should be taken to warrant to the assignee that the assignor will do nothing to prejudice the assignation.

(c) In assigning a claim, whether for value or other than for value, the assignor should not be taken to warrant to the assignee that the debtor will perform to the assignee.

(d) These rules should also apply to any contract or unilateral undertaking which the assignation implements.

(e) These rules should be subject to contrary agreement by the parties.

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[52] See Reid, *Property* para 717 and Jayathilaka, "The Warrandices Implied in the Sale of a Claim to Payment" at 106-107. See also *Waitch v Darling* (1621) Mor 16573.
[53] See Reid, *Property* para 717.
[54] See eg Stair 2.3.46.
[55] See also Jayathilaka, "The Warrandices Implied in the Sale of a Claim to Payment" at 107–111. See also the French Civil Code art 1326.
[56] See Reid, *Property* para 719 and Jayathilaka, "The Warrandices Implied in the Sale of a Claim to Payment" at 114–115.

(f) The common law rules on warrandice in relation to the assignation of claims should be abolished.

(Draft Bill, ss 10 and 17(1)(d))

Assignation in security

13.44 Our recommendations on assignation of claims apply also to assignations in security of claims. It may be worth saying a little more on this subject here.

13.45 First, the alternative of registration instead of intimation would help facilitate assignations in security in relation to claims, making these much easier. Secondly, as we have seen,[57] the definition of "claims" includes rents. The assignation of rents is a very common security transaction which is currently cumbersome because of the need for intimation. Thirdly, for reasons explained more fully later in this Report, we recommend that for the moment at least it is not possible for the new security (the statutory pledge) to be granted in respect of claims.[58] This means that the assignation in security would remain the appropriate form of security in respect of this type of incorporeal moveable property. Fourthly, the clarification of the law which we recommend, namely that a notice of intimation can instruct the debtor to perform to the assignor rather than to the assignee, would help facilitate assignations in security as the parties will only want performance to be made to the assignee on default.[59] Fifthly, assignations in security granted by companies etc. would continue to require to be registered under the company charges registration scheme.[60] Thus, such an assignation would require (1) intimation or registration in the RoA and (2) registration in the Companies Register.

The Cape Town Convention

13.46 The Cape Town Convention on International Interests in Mobile Equipment came into force in the United Kingdom in respect of aircraft objects on 1 November 2015.[61] We say more on this below in volume 2. The Convention provides for a right in security known as an "international interest" which is recognised in the countries that have acceded to the Convention. It has some special rules in relation to the assignation[62] of a right associated with an international interest.[63] Such a right is known as an "associated right". A "claim" within the meaning of our recommendations could qualify as such a right.[64] Therefore our general rules on assignation of claims require to be made subject to these special rules. We recommend:

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[57] See paras 4.13–4.14 above.
[58] See Chapter 22 below.
[59] See paras 5.58–5.61 above.
[60] Companies Act 2006 Part 25.
[61] In terms of The International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015 (SI 2015/912). On the Convention, see R Goode, *Convention on International Interests in Mobile Equipment and Protocol Thereto on Matters Specific to Aircraft Equipment Official Commentary* (revd ed, 2008).
[62] The Convention uses the term "assignment". This is defined as "assignation" for Scotland under reg 35 of the 2015 Regulations.
[63] See regulations 27 to 35 of the 2015 Regulations. For example, under regulation 27 an assignment of an associated right automatically transfers the international interest related to that right.
[64] "Associated rights" are defined as "all rights to payment or other performance by the debtor under an agreement which are secured by or associated with the aircraft object".

68. The general provisions on assignation of claims should be without prejudice to the application, as respects the assignment and acquisition of associated rights, of the International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015.

(Draft Bill, s 18)

Codification

13.47 In the Discussion Paper, we asked consultees whether codification of the law of assignation should be an objective of the moveable transactions project.[65] We noted that the arguments against codification would be the usual arguments – achieving this would be time-consuming, there would be disputes as to its interpretation, drafting errors would be discovered, and even if it were to be done perfectly, the real gain would be small.[66] The arguments in favour of codification would include that it would make the law clearer and more accessible. We said that a middle view would be that whilst codification would be desirable, it would be better to proceed in two stages. These were to reform the law first, and then, once the reforms had bedded down and any problems had come to light, to codify as a second step.

13.48 Consultees who responded to this question were unanimous that codification should not be attempted in this Report. While several thought it desirable in the longer term, they believed that more limited reform in the short term is what is needed.

13.49 We therefore recommend:

69. At the present time the law of assignation of claims should not be codified.

[65] Discussion Paper, para 14.80.

[66] On the general challenges of codifying, see G Gretton, "Of Law Commissioning" (2013) 17 EdinLR 119 at 131–133 and G L Gretton, "The Duty to Make the Law More Accessible? The Two C-Words" in M Dyson, J Lee and S Wilson Stark (eds), *Fifty Years of the Commissions: The Dynamics of Law Reform* (2016) 89 at 93–95.

Chapter 14 Financial collateral

Introduction

14.1 Security over financial collateral is the subject of dedicated legislation.[1] The Financial Collateral Directive ("Directive"), dating from 2002[2] and substantially amended in 2009,[3] applies in EU Member States. It has been implemented in the UK by statutory instrument, the Financial Collateral Arrangements (No. 2) Regulations 2003 ("FCARs").[4]

14.2 The Directive aims to achieve a harmonised set of rules on financial collateral in the European Union which enable security over this type of asset to be taken and enforced more easily. But it has been the subject of significant negative comment, notably for its wide scope of application and lack of clarity.[5] Perhaps unsurprisingly, given their basis in the Directive, the FCARs have similarly been criticised, both generally[6] and in relation to how they apply to Scottish law.[7] Dr Ross Anderson has written: "Few legislative instruments are as difficult to follow as the Financial Collateral Directive; and there can be few examples of legislation implementing a European Directive as unsatisfactory as the attempts by way of the [FCARs] to implement the [Directive] into Scots law."[8]

14.3 In this chapter we attempt to provide an overview of the legislative framework in relation to financial collateral, before setting out the recommendations necessary to make our scheme comply with it in relation to where financial collateral is the subject of an assignation in security. The approach taken in the Discussion Paper was that no special rules were required.[9] As a result, no specific questions on financial collateral were addressed to consultees. On looking into the matter further and with the assistance of our

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[1] See generally Yeowart and Parsons, *The Law of Financial Collateral*; Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* ch 3; Calnan, *Taking Security* paras 3.288–3.300; J Benjamin, "Securities Collateral", in De Lacy (ed), *The Reform of UK Personal Property Security Law* 223–269. There is also much of value in Law Commission, Company Security Interests (Law Com No 296, 2005) Part 5.

[2] Directive 2002/47/EC on financial collateral arrangements.

[3] Directive 2009/44/EC amending Directive 98/26/EC on settlement finality in payment and securities settlement systems and Directive 2002/47/EC on financial collateral arrangements as regards linked systems and credit claims. (For the European Commission Report leading to the amending directive see http://ec.europa.eu/internal_market/financial-markets/docs/collateral/fcd_report_en.pdf.)

[4] Financial Collateral Arrangements (No 2) Regulations 2003 (SI 2003/3226) as amended by the Financial Markets and Insolvency (Settlement Finality and Financial Collateral Arrangements) (Amendment) Regulations 2010 (SI 2010/2993). One of the reasons for the 2010 amendments was that there were problems with the original version of the Regulations as regards Scotland. See H Patrick, "The Financial Collateral Arrangements Regulations: some Scottish issues" 2009 Law and Financial Markets Review 532.

[5] See G L Gretton, "Financial Collateral and the Fundamentals of Secured Transactions" (2006) 10 EdinLR 209; L Gullifer, "What Should We Do about Financial Collateral?" (2012) 65 Current Legal Problems 377 and L Gullifer, "Compulsory Central Clearing of OTC Derivatives: The Changing Face of the Provision of Collateral" in L Gullifer and S Vogenauer (eds), *English and European Perspectives on Contract and Commercial Law: Essays in Honour of Hugh Beale* (2014) at 379–380.

[6] Yeowart and Parsons, *The Law of Financial Collateral* Appendix 1 lists 29 shortcomings and uncertainties. See also the sources referred to in the previous footnote.

[7] See Gretton, "Financial Collateral and the Fundamentals of Secured Transactions" (above).

[8] R G Anderson, "Security over bank accounts in Scots law" 2010 Law and Financial Markets Review 593 at 597.

[9] Discussion Paper, paras 2.10–2.25.

advisory group,[10] we consider now that we need to make express provision in circumstances where the Directive may be applicable.[11]

14.4 An alternative approach, suggested to us by Professor Gretton, was simply to have a provision in our draft Bill stating that it is subject to the Directive. While there are attractions in such an approach, we do not think that it would make the draft Bill sufficiently accessible.

14.5 It remains to be seen what the legal consequences for the application of the Directive are to be in the light of the pending withdrawal of the UK from the EU.

What is financial collateral?

14.6 The Directive has a threefold definition of "financial collateral" as "cash, financial instruments or credit claims".[12]

14.7 "Cash" means, not cash such as bank notes, but "money credited to an account in any currency, or similar claims for the repayment of money, such as money market deposits."[13] Thus it includes a claim to have money repaid if that money has been deposited with a financial institution to be invested in a money market.[14]

14.8 "Financial instruments" are defined as:

> "Shares in companies and other securities equivalent to shares in companies and bonds and other forms of debt instruments if these are negotiable on the capital market, and any other securities which are normally dealt in and which give the right to acquire any such shares, bonds or other securities by subscription, purchase or exchange or which give rise to a cash settlement (excluding instruments of payment), including units in collective investment undertakings, money market instruments and claims relating to or rights in or in respect of any of the foregoing."[15]

14.9 This can be seen to be a broad category, in particular with its inclusion of shares in companies (both certificated and uncertificated[16]). Intermediated securities are also included. This is where shares are held by an intermediary on behalf of an investor.[17]

14.10 "Credit claims" are defined as "pecuniary claims arising out of an agreement whereby a credit institution, as defined in Article 4(1)(1) of Regulation (EU) 575/2013 of the European Parliament and of the Council of 26 June 2013, and including the institutions listed in Article 2(5)(2) to (23) of Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013, grants credit in the form of a loan."[18] Thus if a bank lends Jack £10,000, the bank has a "credit claim". But if a trading company is owed £10,000 by one of its customers

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[10] We are particularly grateful here to Professor George Gretton, Dr Hamish Patrick and Stephen Phillips.
[11] This was also Professor Hugh Beale's view in response to the Discussion Paper. See H Beale, "A View from England" (2012) 16 EdinLR 278 at 281–282.
[12] Directive Art 1(4).
[13] Directive Art 2(1)(d). See too the FCARs reg 3(1).
[14] Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 3.17.
[15] Directive Art 2(1)(e). See too the FCARs reg 3(1).
[16] Dealings in uncertificated shares are carried out electronically under the CREST system. See the Uncertificated Securities Regulations 2001 (SI 2001/3755).
[17] See Discussion Paper, para 7.15 and Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 3.25.
[18] FCARs reg 3(1) as amended by the Capital Requirements Regulations 2013 (SI 2013/3115). For the Directive, see Art 2(1)(o) introduced by Directive 2009/44/EC.

in respect of goods sold, the company does not have a "credit claim." Nor is there a credit claim if Nicola borrows the money not from the bank but from her friend Oliver.

14.11 The Directive therefore does not cover land, or intellectual property, or corporeal moveable property. Its scope is limited to certain types of incorporeal moveable property.

14.12 Professor Louise Gullifer has identified the core attribute of the definition of financial collateral in the Directive as liquidity.[19] Thus it comprises assets which can quickly and easily be transformed into money. The result is that the collateral is often not seen so much as a back-up if payment under the secured obligation is not made, but rather as a form of payment itself, for example by invoking the doctrine of compensation (set-off). For example, imagine that A Ltd lends B Ltd £10,000. In respect of the obligation to repay, B Ltd grants A Ltd security over the sums in a bank account which it holds. B Ltd defaults on repayment and at that time there is £2,000 in that bank account. A Ltd can set off that amount against the outstanding amount owed to it by B Ltd.

14.13 Security over financial collateral is of crucial economic importance.[20] The liquid assets can be used to reduce major systemic risk on the wholesale financial markets[21] and on that basis it is considered necessary to have special rules.[22]

What is a financial collateral arrangement?

14.14 The Directive sets out two types of financial collateral arrangement: (a) a title transfer financial collateral arrangement; and (b) a security financial collateral arrangement.

Title transfer financial collateral arrangement (TTFCA)

14.15 Article 2(1) of the Directive provides that a "title transfer financial collateral arrangement" means:

> "an arrangement, including repurchase agreements, under which a collateral provider transfers full ownership of, or full entitlement to, financial collateral to a collateral taker for the purpose of securing or otherwise covering the performance of relevant financial obligations".

14.16 The corresponding definition in the FCARs is:

> "an agreement or arrangement, including a repurchase agreement, evidenced in writing, where
>
> (a) the purpose of the agreement or arrangement is to secure or otherwise cover the relevant financial obligations owed to the collateral-taker;
>
> (b) the collateral-provider transfers legal and beneficial ownership in financial collateral to a collateral-taker on terms that when the relevant financial obligations are discharged the collateral-taker must transfer legal and

[19] Gullifer, "What Should We Do about Financial Collateral?" (n 5) at 380.
[20] See D Murphy, "The rising risks and roles of financial collateral" 2014 Journal of International Business and Financial Law 3.
[21] The wholesale financial markets are those used by bodies engaging in large-scale financial transactions, typically larger companies, financial institutions and governments.
[22] Gullifer, "What Should We Do about Financial Collateral?" (n 5) at 400–401.

beneficial ownership of equivalent financial collateral to the collateral-provider; and

(c) the collateral-provider and the collateral-taker are both non-natural persons".[23]

14.17 We discuss aspects of these definitions below, but it can be seen that the essence of a TTFCA is that the collateral is transferred to the creditor. The classic example is a "repo" ("repurchase agreement"). Here one party sells market securities[24] to another for cash and agrees to repurchase equivalent securities subsequently at the original sale price plus a premium representing interest on the price (sometimes called the "repo rate").[25]

14.18 As financial collateral in Scottish law terms is incorporeal moveable property and as under our current law the method of giving security over such property is to transfer it,[26] it would seem to follow that any financial collateral arrangement must be a TTFCA.[27] There is an exception to this: the floating charge.[28] But, such is the opaque nature of the legislation, it is not impossible that an assignation in security could also be regarded as a security financial collateral arrangement. Thus the FCARs now disapply the need to register at Companies House in Scotland "any charge created or arising under a financial collateral arrangement".[29] Thus it is not limited to TTFCAs. In fact the original version of the Regulations was limited to security financial collateral arrangements.[30]

14.19 Article 6 of the Directive requires that a TTFCA "can take effect in accordance with its terms". It is therefore not possible for national legislation to recharacterise it as a security right.

Security financial collateral arrangement (SFCA)

14.20 The Directive states that a "security financial collateral arrangement" means:

> "an arrangement under which a collateral provider provides financial collateral by way of security to or in favour of a collateral taker, and where the full or qualified ownership of, or full entitlement to, the financial collateral remains with the collateral provider when the security right is established".[31]

14.21 The corresponding definition in the FCARs is:

> "an agreement or arrangement, evidenced in writing, where

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[23] FCARs reg 3(1). The term "legal and beneficial ownership" are unfamiliar in Scottish law.
[24] Such as government bonds.
[25] A survey by the International Capital Market Association in December 2014 which was responded to by the major players in the repo market in Europe valued outstanding repo transactions at €5,500 billion. See http://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/short-term-markets/Repo-Markets/repo/.
[26] See Chapter 3 above. See also Yeowart and Parsons, *The Law of Financial Collateral* para 23.06 (H Patrick).
[27] Gretton, "Financial Collateral and the Fundamentals of Secured Transactions" at 214. See also Yeowart and Parsons, *The Law of Financial Collateral* paras 6.07 and 7.25.
[28] A further exception may be bearer instruments which can be pledged. But whether this is a true pledge or a transfer is unclear. See Steven, *Pledge and Lien* paras 5-07 to 5-09.
[29] FCARs reg 4(4) as amended.
[30] These were amended by the Financial Markets and Insolvency (Settlement Finality and Financial Collateral Arrangements) (Amendment) Regulations 2010 (SI 2010/2993). See H Patrick, "The Financial Collateral Arrangement Regulations: some Scottish issues" (2009) 3 Law and Financial Markets Review 532.
[31] Directive Art 2(1).

(a) the purpose of the agreement or arrangement is to secure the relevant financial obligations owed to the collateral-taker;

(b) the collateral-provider creates or there arises a security interest in financial collateral to secure those obligations;

(c) the financial collateral is delivered, transferred, held, registered or otherwise designated so as to be in the possession or under the control of the collateral taker or a person acting on its behalf; any right of the collateral-provider to substitute financial collateral of the same or greater value or withdraw excess financial collateral or to collect the proceeds of credit claims until further notice shall not prevent the financial collateral being in the possession or under the control of the collateral-taker; and

(d) the collateral-provider and the collateral-taker are both non-natural persons".[32]

14.22 We discuss aspects of these definitions below, but it appears that in an SFCA the collateral is not transferred to the secured creditor. Rather, title is retained by the provider and the secured creditor obtains a subordinate real right, as in pledge of a corporeal moveable.[33] But such is the general opaque nature of the Directive and FCARs it is impossible to be sure that an assignation in security of a claim would not be classified as an SFCA.

Parties

14.23 The Directive provides that the collateral-taker and the collateral provider must each belong to one of a number of categories.[34] Categories (a) to (d) comprise public authorities, such as central banks, and commercial entities meeting certain requirements, such as authorised banks and clearing houses. Category (e) is any person other than a natural person. Thus any entity in Categories (a) to (d) would also qualify in Category (e).

14.24 The Directive applies only if both of the parties fall into Category (e) and at least one of the parties falls into Categories (a) to (d). The FCARs[35] go further, so that a financial collateral arrangement between two private companies, for example a transaction involving shares, would be caught. In *R (Cukorova Finance International Ltd) v HM Treasury*[36] a challenge to the Regulations in the High Court of England and Wales on the basis that this is not justified by the Directive was unsuccessful. The judge, Moses LJ, did not accept the argument that the Directive's purpose was to ensure stability on the wholesale financial markets rather than being of more general application. In the subsequent Supreme Court case of *The United States of America v Nolan*,[37] which concerned different Regulations, Lord Mance expressed doubts as to whether Moses LJ had reached the correct conclusion and the matter remains controversial.[38] The broader application of the FCARs compared with the

[32] FCARs reg 3(1) as amended.
[33] A floating charge would also in principle be a SFCA, but the requirement of control is unlikely to be satisfied in the case of that security.
[34] Directive Art 1(2).
[35] FCARs reg 3(1).
[36] [2008] EWHC 2567 (Admin).
[37] [2015] UKSC 63.
[38] [2015] UKSC 63 at paras [67]–[69]. See Yeowart and Parsons, *The Law of Financial Collateral* para 2.29.

Directive is also difficult to justify in policy terms. It seems unlikely that transactions between two private companies would result in systemic risk on the wholesale financial markets.[39]

Disapplication of formalities

General

14.25 The Directive disapplies certain formalities in relation to security over financial collateral. Article 3(1) provides:[40]

> "Member States shall not require that the creation, validity, perfection,[41] enforceability or admissibility in evidence of a financial collateral arrangement or the provision of financial collateral under a financial collateral arrangement be dependent on the performance of any formal act.
>
> …When credit claims are provided as financial collateral, Member States shall not require that the creation, validity, perfection, priority, enforceability or admissibility in evidence[42] of such financial collateral be dependent on the performance of any formal act such as the registration or the notification of the debtor of the credit claim provided as collateral. *However, Member States may require* the performance of a formal act, such as *registration or notification, for purposes of perfection, priority, enforceability* or admissibility in evidence against the debtor or third parties."[43]

14.26 The first of these paragraphs is a general provision prohibiting any requirement, on the part of national law, for any "formal act". There is no definition of this term in the Directive, but Recital 10 gives some examples:

> "… the execution of any document in a specific form or in a particular manner, the making of any filing with an official or public body or registration in a public register, advertisement in a newspaper or journal, in an official register or publication or in any other matter, notification to a public officer or the provision of evidence in a particular form as to the date of execution of a document or instrument, the amount of the relevant financial obligations or any other matter."

14.27 Thus the FCARs disapply the usual requirement of registration in the Companies Register for security granted by a company where the security is over financial collateral.[44]

14.28 The second paragraph of Article 3(1) referred to above is a special and more detailed provision in the case where the financial collateral consists of "credit claims". The second sentence of the second paragraph appears to take away most of the force of the first sentence. Thus in respect of "credit claims" a formal act apparently can be required for perfection, priority and enforceability but *not* for creation or validity.

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[39] See Gullifer, "What Should We Do about Financial Collateral?" (n 5) at 401ff.
[40] Directive Art 3(1).
[41] The meaning of this term, which is also used in the next paragraph, is uncertain. Possibly it has the UCC meaning. But the French and German terms ("*conclusion*" and "*Abschluss*") do not fit such a meaning. When Recital 9 speaks of perfection, the French term is "*opposabilité*", and yet that latter term matches, in Art 3, not "perfection" but "enforceability".
[42] This list is different from the list in the previous paragraph and both are different from the list in the last sentence of the second paragraph. The significance of these differences is unclear.
[43] Emphasis added.
[44] FCARs reg 4(4).

14.29 The Directive does not unconditionally sweep away formality requirements. It only does so where (a) the financial collateral arrangement and its provision are evidenced in writing and (b) the collateral-taker (creditor) has "possession" or "control" of the collateral.[45]

Writing

14.30 The Directive requires both that the financial collateral arrangement itself and the provision of the collateral are evidenced in writing.[46] "Writing" includes recording by electronic means and any other durable medium."[47] As well as e-mails, recordings of telephone conversations will qualify.[48] Care therefore requires to be taken with bearer instruments that both the security agreement and delivery of the instruments are duly recorded.

The requirement for possession or control

14.31 Article 1(5) provides that "This Directive applies to financial collateral *once it has been provided*." This is explained by Article 2(2), which states:

> "References in this Directive to financial collateral being 'provided', or to the 'provision' of financial collateral, are to the financial collateral being *delivered, transferred, held, registered* or otherwise designated so as to be in the possession or under the control of the collateral taker or of a person acting on the collateral taker's behalf."[49]

14.32 As Professor Gretton has noted,[50] the FCARs appear to have been drafted on the basis that the need for "provision" only applies to SFCAs and not TTFCAs. This, however, seems not to take account of the breadth of Article 1(5).

14.33 Recital 9 of the Directive states: "… the only perfection requirement regarding parties which national law may impose in respect of financial collateral should be that the financial collateral is *under the control of the collateral taker* or of a person acting on the collateral taker's behalf…"[51] Recital 10 states that "this Directive cover[s] only those financial collateral arrangements which provide for some form of *dispossession, ie the provision* of the financial collateral…"

14.34 The Directive does not further define "possession" or "control". This was originally the position in the FCARs. In *Gray v G-T-P Group Ltd, Re F2G Realisations Ltd (in liquidation)*[52] Vos J doubted the relevance of "possession" in relation to intangible (incorporeal) property. He concluded that for a collateral-taker to have control, the collateral provider must be prevented legally and (probably) practically from transacting with the collateral.[53] The control thus required may be termed "negative control", as opposed to

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[45] See paras 14.31–14.36 below.
[46] Directive Arts 1(5) and 3(2). On the meaning of "provision" see the next paragraph.
[47] Directive Art 2(3). What is meant by "other durable medium" is unclear. See Gretton, "Financial Collateral and the Fundamentals of Secured Transactions" at 233.
[48] Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 3.30.
[49] Emphasis added.
[50] Gretton, "Financial Collateral and the Fundamentals of Secured Transactions" (n 5) at 226–227.
[51] Emphasis added.
[52] [2010] EWHC 1772 (Ch).
[53] For a full analysis, see Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 3.33ff. See also R Parsons and M Dening, "Financial collateral – an opportunity missed" (2011) 5 Law and

"positive control", where the collateral-taker is legally and practically able to take or dispose of the collateral without requiring to involve the debtor.[54] The *Gray* case involved a floating charge and the argument was that there was the necessary possession or control to mean that the exemption from registering SFCAs under the company charges registration scheme applied.[55] The argument was unsuccessful.

14.35 In 2011 the FCARs were amended to provide that:

> ""possession" of financial collateral in the form of cash or financial instruments includes the case where financial collateral has been credited to an account in the name of the collateral-taker or a person acting on his behalf (whether or not the collateral-taker, or person acting on his behalf, has credited the financial collateral to an account in the name of the collateral-provider on his, or that person's, books) provided that any rights the collateral-provider may have in relation to that financial collateral are limited to the right to substitute financial collateral of the same or greater value or to withdraw excess financial collateral."[56]

14.36 This was largely prompted by Vos J's interpretation of "possession". Furthermore, in the subsequent case of *Re Lehman Brothers International (Europe) (in administration)*,[57] Briggs J took a different approach, holding that it would be wrong to limit "possession" in a way that excludes intangibles.[58] For him, what was essential was that there was sufficient control or possession on the part of the collateral taker for the collateral provider to be "dispossessed".[59] In some cases the collateral may be so "sufficiently clearly in the possession of the collateral taker that no further investigation of its rights of control is necessary."[60] But, notwithstanding this decision, there continues to be uncertainty about what is required to establish possession or control.[61]

Assignation of claims

14.37 Under current Scottish law if B Ltd wishes to transfer to C Ltd a claim, such as a right to payment, which it has against A Ltd there requires to be (a) an assignation of the claim, followed by (b) intimation to A Ltd.[62] We recommend in this Report that the requirement for intimation is retained but the alternative of registration of the assignation in the Register of Assignations should be introduced.[63] A claim, however, may satisfy the definition of "financial collateral" in the Directive, for example it could be a credit claim (as defined). The question is whether there requires to be a special rule in such cases which would apply

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Financial Markets Review 164 at 166–168 and T Anderson, "Dilemmas of possession and control" 2011 Journal of International Banking and Financial Law 431.

[54] Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 3.45.

[55] Now FCARs reg 4(4).

[56] FCARs reg 3(2), as amended, with effect from 6 April 2011, by the Financial Markets and Insolvency (Settlement Finality and Financial Collateral Arrangements) (Amendment) Regulations 2010 (SI 2010/2993).

[57] [2012] EWHC 2997 (Ch). See E Chell, C Meinertz and J Walter, "Possession and control: financial collateral remains a Gray area" 2013 Journal of International Business and Financial Law 43.

[58] [2012] EWHC 2997 at para 131.

[59] [2012] EWHC 2997 at para 136.

[60] [2012] EWHC 2997 at para 136. Perhaps an example of this would be bearer securities in the possession of the collateral-taker.

[61] The Law Commission for England and Wales, Company Security Interests (Law Com No 296, 2005) Part 5 recommended that "control" be defined for the purposes of its recommended new scheme on security over personal property but accepted that it was impossible to define the term for the purposes of the Directive because this is a matter of European Union law.

[62] See para 3.7 above.

[63] See Chapter 6 above.

where an assignation (in security) is within the scope of the Directive, in other words is a financial collateral arrangement.

14.38 The FCARs expressly disapply in Scotland "an act [that] is required as a condition for transferring, creating or enforcing a right in security over any book entry securities collateral".[64] "Book entry securities collateral" is defined as "financial collateral subject to a financial collateral arrangement which consists of financial instruments, title to which is evidenced by entries in a register or account maintained by or on behalf of an intermediary".[65] "Act" is defined as "(a) any act other than an entry on a register or account maintained by or on behalf of an intermediary which evidences title to the book entry securities collateral [and] (b) includes the entering of the collateral-taker's name in a company's register of members."[66] These provisions clearly only apply to intermediated securities. But, as Professor Gretton has demonstrated, their rationale, including their Scotland-only application, is uncertain.[67] It is possible that the objective is to remove the requirement of intimation to the intermediary where there is an assignation of an intermediated security which qualifies as a financial collateral arrangement. The requirements of the current law for intimation are commercially unworkable as intermediated securities are held electronically.[68]

14.39 In England and Wales, there is a distinction between legal assignments, which require notification (intimation) to transfer the claim,[69] and equitable assignments, which do not.[70] The FCARs do not disapply the requirement for intimation of legal assignments on the basis that this is not required by the Directive.[71]

14.40 Our recommendations would allow an assignation in security of a claim to be completed by registration in the RoA. Registration, however, is a type of "formal act" which the Directive seeks to disapply. But the alternative of intimation would be available and the requirements for intimation would be less onerous under the current law with intimation by electronic notice being possible. Thus it can be argued that no special rule is required. It is impossible to be certain how strong such an argument is. In particular, there is a distinction with English law because equitable assignment (with no intimation or registration) is recognised there. Thus, on one view, intimation only matters in English law for priority purposes because an assignment will be effective to transfer a claim in equity without intimation. In Scotland under our recommendations, unless there were registration in the RoA, intimation would be required for transfer. Intimation would therefore not solely be a priority issue.[72]

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[64] FCARs reg 6(1).
[65] FCARs reg 3(1).
[66] FCARs reg 6(2).
[67] Gretton, "Financial Collateral and the Fundamentals of Secured Transactions" (n 5) at 234–236.
[68] Such as the need under the Transmission of Moveable Property (Scotland) Act 1862 for a copy of the assignation document to be intimated. See paras 3.9–3.10 and 5.40–5.44 above.
[69] Law of Property Act 1925 s 136.
[70] But equitable assignments are vulnerable to being trumped by a subsequent assignment which is intimated: *Dearle v Hall* (1828) 3 Russ 1. On the rule see J de Lacy, "Reflections on the Ambit of the Rule in *Dearle v Hall*" (1999) 28 Anglo-American Law Journal 87 and 197.
[71] See Gretton, "Financial Collateral and the Fundamentals of Secured Transactions" (n 5) at 233–234.
[72] Yeowart and Parsons, *The Law of Financial Collateral* para 23.50 (H Patrick).

14.41 The best solution would be for the meaning of the Directive on this issue to be clarified, along with other uncertainties under this legislation which have been identified. But this would require to be done at a European Union level.[73] We have therefore concluded that in the meantime we require to take a cautious approach. This means excluding the requirement for intimation or registration in the RoA where an assignation of a claim amounts to a TTFCA or SFCA. Instead, we consider that in such circumstances the assignation could be completed by the financial collateral in question coming into the possession of, or under the control of the collateral-taker (assignee) or a person acting on the collateral-taker's behalf. As we saw above, it is a requirement under the Directive that the collateral must be provided to the collateral-taker so that the collateral-taker receives possession or control of it.[74] On the other hand, in the FCARs this is only a requirement for an SFCA, a point noted by Professor Hugh Beale and Professor Louise Gullifer in their response to our draft Bill consultation of July 2017. But there is nothing in the Directive or in the FCARs to prevent such a rule being imposed in relation to a TTFCA. The alternative of merely requiring an assignation document for a TTFCA would not satisfy the requirement for an external act in Scottish property law in relation to transfer. A TTFCA has the priority of an English legal rather than equitable assignment and therefore, in our view, requiring the additional step of possession or control is appropriate.

14.42 Where an assignation constitutes a TTFCA or SFCA, it is also necessary in order to comply with the Directive to disapply the requirement for an assignation to be executed or signed electronically.[75] The assignation document merely requires to be created as writing transcribed by electronic or other means in a durable medium, or as sounds recorded in such a medium. But the other ordinary transfer rules in relation to a claim would remain applicable, in particular that the assignor (collateral-provider) holds it, that the claim is identifiable as a claim to which the assignation document relates and that any condition which must be satisfied in order for there to be transfer is duly satisfied.

14.43 We therefore recommend:

70. (a) If an assignation document evidences a security financial collateral arrangement or a title transfer financial collateral arrangement (as defined in regulation 3 of the Financial Collateral Arrangements (No. 2) Regulations 2003) in respect of a claim, then the transfer of that claim should require either (i) intimation to the debtor or registration in the Register of Assignations, or (ii) the financial collateral in question to come into the possession of, or under the control of, the collateral-taker or a person authorised to act on the collateral-taker's behalf.

(b) In case (ii) the assignation document need not be executed or signed electronically and may be created as writing transcribed by electronic or other means in a durable medium, or as sounds recorded in such a medium.

(Draft Bill, s 4)

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[73] The departure of the UK from the European Union will of course have consequences here.
[74] See paras 14.31–14.36 above.
[75] See paras 4.15–4.20 and 14.30 above.

Chapter 15 International private law

Introduction

15.1 Where a case involves more than one legal system the branch of law known as international private law determines which set of legal rules apply (the applicable law), and which country's courts have the right to hear and determine a given matter (jurisdiction).

15.2 In the Discussion Paper we noted that in principle it would be possible to address the international private law aspects of moveable transactions as part of the project. But we took the view that cross-border issues should be left to existing international private law rules to determine when Scottish law applies and when it does not. We considered that the project should confine itself to the substantive Scottish law of moveable transactions to keep it within manageable bounds.[1] This approach was, however, questioned by some consultees.[2] We have therefore decided to review the matter here. This chapter therefore outlines the various international private law issues which arise in relation to assignation of claims. It looks also briefly at the issue of jurisdiction.

Legislative background

15.3 This area is heavily regulated by EU law, limiting national competence to legislate. At the time of writing the consequences of Brexit in relation to applicable law and jurisdiction remain to be worked out.[3] We therefore proceed on the basis that EU law remains binding.

15.4 The Brussels Convention of 1968 on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters created a new harmonised framework for allocating jurisdiction to courts of the then European Economic Community Members. The introduction of this Convention led the Belgian Government to propose that the Member States should collaborate on the basis of a draft convention to harmonise their international private law rules, which it saw as "a natural sequel to the Convention on jurisdiction and the enforcement of judgments."[4]

15.5 Three decades later, the Treaty of Amsterdam 1997[5] introduced new Community competence in the area of judicial co-operation on civil matters and the recognition of foreign judgments, under Articles 61(c) and 67(1) of the EC Treaty, facilitating the conversion of the 1968 Convention into a new Regulation. This sequence of events resulted in two

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[1] Discussion Paper, para 1.16.
[2] For example, Scott Wortley considered that international private law issues should have been given a greater treatment in his response to the Discussion Paper.
[3] See A Dickinson, "Back to the future: the UK's EU exit and the conflict of laws" (2016) 12 Journal of Private International Law 195.
[4] Report on the Convention on the law applicable to contractual obligations by M Giuliano and P Lagarde, Official Journal C 282, 31/10/1980 P.00010 – 0050 at 4–5.
[5] The content of which can be found at: http://europa.eu/eu-law/decision-making/treaties/pdf/treaty_of_amsterdam/treaty_of_amsterdam_en.pdf

Regulations of importance for present purposes: the Brussels I Regulation (recast)[6] and the Rome I Regulation.[7]

15.6 The result is that the UK has limited competence to legislate in areas of international private law. Reform of the rules on jurisdiction and choice of court, for example, are restricted to conflicts involving non-EU member states and intra-UK cases.[8] This is because the Brussels regime only applies as between persons domiciled in EU member states. Further, jurisdictional rules for both intra-UK cases and those involving countries outwith the EU are relatively settled and can be found in the Schedules to the Civil Jurisdictions and Judgments Act 1982.[9]

15.7 Unlike the Brussels regime, the Rome I Regulation is of universal application and has no domicile requirement for litigating parties. Thus, determination of the law applicable to contractual obligations in civil and commercial matters must be made by following the rules in the Rome I Regulation, unless the subject matter falls outwith its scope.[10] One important caveat is that Rome I is overridden by any uniform law convention.[11] This includes the 1988 UNIDROIT Convention on International Factoring which has limited application in the realm of assignations of claims. It applies only where those States in which the factor has its place of business are Contracting States; and/or where both the contract of sale of goods and the factoring contract are governed by the law of a Contracting State.[12] If the first condition is met then the Convention will directly apply. If not, the Rome I Regulation will determine whether the second condition is met as a preliminary issue.[13]

15.8 The assignation of claims is within the scope of the Regulation and therefore precludes any Scottish (or, for that matter, UK) legislation on the applicable law in such cases. Moreover, Article 14 of the Rome I Regulation on voluntary assignments appears to determine both the contractual and proprietary effects of such transactions.

Applicable law: outright transfer of incorporeal moveable property

Rome I: introduction

15.9 The assignation of claims has become very important within the financial services industry, for example in factoring and securitisation arrangements.[14] As mentioned in the preceding paragraphs, this area is generally subject to the Rome I Regulation.[15] Article 14

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[6] Regulation (EU) 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (recast). This recently replaced Council Regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, which in turn replaced the 1968 Convention on jurisdiction and the enforcement of judgments in civil and commercial matters (Brussels Convention/Jurisdiction and Judgments Convention) (Brussels, 27 September 1968).

[7] Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations.

[8] Although see also the Lugano Convention 2007 which creates the same limitations for certain EFTA countries.

[9] Schedules 4 and 8.

[10] Rome I Regulation, Article 1.

[11] Rome I Regulation, Article 25.

[12] UNIDROIT Convention on International Factoring, Ottawa 28 May 1988, available at www.unidroit.org. While the UK was a signatory, it has not acceded to the Convention.

[13] See M Mankowski, *European Commentaries on Private International Law: Rome I Regulation* (2017) 752.

[14] See para 3.16 above.

[15] For a brief overview of the history of international instruments affecting assignations in the European context, see W G Ringe, "The Law of Assignment in European Contract Law" in L Gullifer and S Vogenauer (eds), *English*

regulates assignments of, and security over, claims. The definition of 'claims' is wide and includes receiving sums of money, as well as delivering goods or rendering services.[16] As assignation is the method of transferring incorporeal moveable property in Scotland,[17] for Scottish purposes "assignment" must mean assignation. Article 14 provides:

> "1. The relationship between assignor and assignee under a voluntary assignment or contractual subrogation of a claim against another person (the debtor) shall be governed by the law that applies to the contract between the assignor and assignee under this Regulation.
>
> 2. The law governing the assigned or subrogated claim shall determine its assignability, the relationship between the assignee and the debtor, the conditions under which the assignment or subrogation can be invoked against the debtor and whether the debtor's obligations have been discharged.
>
> 3. The concept of assignment in this Article includes outright transfers of claims, transfers of claims by way of security and pledges or other security rights over claims."

15.10 These provisions clearly distinguish questions based on whether they relate to (i) the contract to assign or (ii) the claim being assigned. Under paragraph one, the validity of an assignment *as between* the assignor and assignee is governed by the law applicable to the contract to assign. In contrast, the underlying *assignability* of the claim and the *relationship* between the assignee and debtor are to be governed by the law applicable to the assigned claim.[18] The relationship between the assignor and debtor is governed by the law that creates the obligation between them. From a Scottish property law perspective the concept of an assignment (assignation) taking effect as between the assignor and assignee, but not having effect in a question with other parties is inherently problematic.[19]

15.11 Further, recital 38 of the Regulation states:

> "In the context of voluntary assignment, the term 'relationship' should make it clear that Article 14(1) also applies to the property aspects of an assignment, as between assignor and assignee, in legal orders where such aspects are treated separately from the aspects under the law of obligations. However, the term 'relationship' should not be understood as relating to any relationship that may exist between assignor and assignee. In particular, it should not cover preliminary questions as regards a voluntary assignment or a contractual subrogation. The term should be strictly limited to the aspects which are directly relevant to the voluntary assignment or contractual subrogation in question."

15.12 "Preliminary questions" include the underlying assignability of the claim. Thus, if A contracts with B to assign a claim, whether the claim is assignable in the first place would not necessarily be decided using the same law that applies to all other aspects of the parties' "relationship". Indeed, paragraph 2 would operate in this situation and the underlying

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and European Perspectives on Contract and Commercial Law: Essays in Honour of Hugh Beale (2014) 251 at 253–257.

[16] Mankowski, *European Commentaries on Private International Law: Rome I Regulation* at 754.

[17] See para 3.2 above.

[18] P R Beaumont and P E McEleavy (eds), *Anton's Private International Law* (3rd edn, 2011) 964 ff.

[19] See para 5.17 above.

assignability of the claim would be determined in accordance with the law applying to the original contract from which the debt arose.

Assignability of claim and relationship between assignor and assignee

15.13 The propositions that (i) the assignability of a claim should be determined by the law which governs that claim and (ii) the relationship between an assignor and assignee should be governed by the law under which the contract to assign was formed, are not controversial. These rules do, however, create problematic scenarios which Professor Trevor Hartley describes as the problem of 'relativity'.[20] He points out that the choice of law rules applicable to decide a question are different depending on the parties to the proceedings in which the question arises.

15.14 We have seen that, as between the assignor and assignee, under paragraph 1 of Article 14 the validity of an assignment is governed by the law of the assignment. However where the question of validity of an assignment arises in proceedings between the assignee and the debtor, that question must be decided by the law of the obligation, as per paragraph 2. Professor Hartley gives the example of an assignee suing for payment and the debtor claiming he was never notified.[21] Beyond paragraph 1, recital 38 offers no guidance on how to answer such incidental questions as between the assignee and debtor.

15.15 But in proceedings involving the assignor and assignee, what if the question is not incidental but rather makes up the focal point of litigation? Under paragraph 2 the question of whether or not a claim is assignable is determined by the law of the underlying obligation. But if the assignee sues the assignor because the assigned claim turns out to be unassignable, the applicable law is not so clear; paragraph 1 clearly states that the relationship between the assignor and assignee is to be regulated by the law governing the assignation.[22] It seems to us that the same law should be applicable to a given question, irrespective of which parties raise the proceedings. Further, as already noted, under Scottish law an assignation is either effective or it is not, rather than potentially being effective between the assignor and assignee, but not with regard to third parties.

15.16 An alternative analysis is that some Member State jurisdictions recognise a difference between the underlying contract and the deed of assignation. Recital 38 therefore attempts, rather ironically, to clarify that the law referred to in Article 14(1) determines the question of whether a deed of assignment in such jurisdictions, independently from or together with the underlying contract, is required to transfer the proprietary rights over the claim.[23] This analysis, however, does nothing to address the concern that an assignation agreement might be valid between the assignor and assignee, but not as between the assignor and debtor. This problem is discussed in more detail below.

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[20] T C Hartley, "Choice of law regarding the voluntary assignment of contractual obligations under the Rome I Regulation" (2011) 60 International and Comparative Law Quarterly 29 at 35 ff.

[21] Hartley, "Choice of law regarding the voluntary assignment of contractual obligations under the Rome I Regulation" at 36.

[22] Hartley, "Choice of law regarding the voluntary assignment of contractual obligations under the Rome I Regulation" at 37. See also H C Sigman and E Kieninger (eds), *Cross-Border Security over Receivables* (2009) 1 at 56–57.

[23] See Mankowski, *European Commentaries on Private International Law: Rome I Regulation* at 756–757.

Contractual and proprietary issues

15.17 Transactions involving incorporeal moveable property (such as claims) tend to cause complex issues of characterisation. In order to ascertain the law applicable to any given issue, a court must first "characterise" the issue by identifying the appropriate area of law. Questions involving incorporeal moveable property may engage both contract law and property law.[24] This is problematic because there are different so-called "connecting factors" which link an issue to a legal system, depending on how the issue is characterised. For example, if the matter is deemed to be contractual in nature, then the Rome I Regulation will apply, and the rule in either paragraph 1 or 2 will operate as the connecting factor.[25] Article 14(3) mitigates this issue somewhat by expressly stating that the Article covers not only outright transfers of claims, but also transfers by way of security, pledges, or other security rights over claims. It does not, however, cover the effects of agreements in a question with third parties, and thus issues of characterisation persist in this context.

15.18 One of the core features of incorporeal moveable property is the lack of a physical presence. As a result it is often most closely associated with the underlying contract. These problems are summarised by Professors Clarkson and Hill:

> "There are two points which should be borne in mind in cases involving the assignment of intangibles. First, as with all property transactions, it is vital to distinguish contractual issues from proprietary ones. One must not fall into the trap of assuming that where an assignment of an intangible is effected by contract, the only question to consider is the validity of the contract. Secondly, in cases involving the assignment of certain types of intangible (in particular, debts) there are two transactions to consider: the first is the transaction which creates the relationship between the debtor and the creditor; the second is the assignment by the creditor to the assignee."[26]

15.19 This problem is an historic one, and many of the leading cases in this area are based on Rome I's predecessor, the Rome Convention.[27] Article 12 of the Convention dealt with voluntary assignation and spoke of the "mutual obligations" of the assignor and assignee. There was no supporting information to clarify precisely whether or not this extended to the proprietary rights of the parties, and in fact this was a conscious decision in order to prevent a lengthy exposition on what 'property rights' meant for the various legal systems of the Member States:

> "First, since the Convention is concerned only with the law applicable to contractual obligations, property rights and intellectual property are not covered by these provisions. An article in the original preliminary draft had expressly so provided. However, the group considered that such a provision would be superfluous in the present text, especially as this would have involved the need to recapitulate the differences existing between the various legal systems of the Community."[28]

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[24] M McParland, *The Rome I Regulation on the Law Applicable to Contractual Obligations* (2015) para 18.08.
[25] See also H Patrick, "Romalpa: the international dimension" 1986 SLT (News) 265 at 267.
[26] J Hill and M Ní Shúilleabháin, *Clarkson & Hill's Conflict of Laws* (5th edn, 2016) 479.
[27] Rome Convention on the Law Applicable to Contractual Obligations (Rome, 19 June 1980).
[28] Report on the Convention on the law applicable to contractual obligations by M Giuliano and P Lagarde, Official Journal C 282, 31/10/1980 P.00010 – 0050 at 10.

15.20 This is, however, somewhat inconsistent with the later commentary on Article 12 in the Giuliano-Lagarde report which states that Article 12(2) covers not only the conditions of transferability of the assignation but also the procedures required to give effect to the assignation in relation to the debtor.[29] This statement implies that the proprietary aspects of the assignor and debtor's relationship are to be governed by Article 12(2), despite the earlier statement to the contrary.

The Raiffeisen *approach*

15.21 The foregoing interpretation heavily influenced the Court of Appeal of England and Wales in the leading case in this area, *Raiffeisen Zentral Bank Osterreich AG v Five Star General Trading LLC (The Mount I)*.[30] There, Lord Justice Mance held that in an insurance contract case, Article 12(2) of the Rome Convention covered "issues both as to whether the debtor owes monies to and must pay the assignee (their 'relationship') and under what 'conditions', for example, as regards the giving of notice."[31] He came to this conclusion by consulting the Giuliano-Lagarde Report on this point and stating:

> "The Rome Convention now views the relevant issue – that is, what steps, by way of notice or otherwise, require to be taken in relation to the debtor for the assignment to take effect as between the assignee and debtor – not as involving any 'property right', but as involving – simply – a contractual issue to be determined by the law governing the obligation assigned."[32]

15.22 This construction does, however, create some difficulties. To accept that procedures required to give effect to an assignation are contractual issues, solely on the basis of the explanatory report to the Rome Convention, appears to ignore the fact that domestic legal systems will continue to characterise the issues as proprietary in nature.

15.23 Lord Brodie confirmed this interpretational difficulty in *Atlantic Telecom GmbH, Noter*[33] when, agreeing with the approach of Lord Justice Mance in *Raiffeisen* that the court must first ask if the issue fell within the scope of the Convention, he stated that:

> "Nevertheless, in characterising the issue raised in this case I am applying Scots law. I am looking at matters from the perspective of a Scots lawyer. I consider that I am entitled to form an impression of the character of the issue from that perspective, just as I am entitled (to the extent that this is a different exercise) to identify what is the issue from that perspective."[34]

15.24 In 2003 the European Commission issued a Green Paper[35] which sought to modernise the Rome Convention and convert it into a Community instrument. It recognised the absence of any rules on the proprietary effects of assignation which led to the new Article 14 and accompanying recital.

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[29] Report on the Convention on the law applicable to contractual obligations by M Giuliano and P Lagarde, Official Journal C 282, 31/10/1980 P.00010 – 0050 at 34–35.
[30] [2001] EWCA Civ 68.
[31] *Raiffeisen Zentral Bank Österreich AG v Five Star General Trading LLC (The Mount I)* [2001] EWCA Civ 68 at para 43.
[32] *Raiffeisen Zentral Bank Österreich AG* at paras 47–48.
[33] 2004 SLT 1031.
[34] 2004 SLT 1031 at 1044.
[35] Green Paper on the conversion of the Rome Convention of 1980 on the law applicable to contractual obligations into a Community instrument and its modernisation (COM (2002) 654 final).

15.25 Articles 14(1) and (2) of the Rome I Regulation are in similar terms to Articles 12(1) and (2) of the Convention, although the term "mutual obligations" has been replaced by "relationship". Unlike its predecessor, this term is defined in recital 38 to the Regulation, and seems to reiterate the judgment in *Raiffeisen* and the Giuliano-Lagarde Report stating that Article 14(1):

> "also applies to the property aspects of an assignment, as between assignor and assignee, in legal orders where such aspects are treated separately from the aspects under the law of obligations."

15.26 The difficulty with recital 38 is that it only relates to the assignor and assignee relationship; there is no equivalent provision for the relationship of the assignee and debtor under Article 14(2).[36] Indeed, this ties in with a wider issue that both Articles 12 and 14 of the Convention and Regulation respectively fail to deal with the question of the law applicable to the effectiveness of the assignation in a question with third parties.[37] This was another issue identified by the European Commission Green Paper, but one that could not be resolved due to an inability to reach a compromise between the law of habitual residence of the assignor at the material time and the law governing the assigned debt. The former option was originally proposed by the European Commission, but was withdrawn from the draft Regulation after it did not find favour with the European Council.[38]

15.27 The inability to reach a consensus on the applicable law for third party effects explains why paragraphs 1 and 2 of Article 14 seem to create Professor Hartley's problem of 'relativity'. The intention of recital 38, drafted when the Commission's proposed rule governing third party effects remained in the draft Regulation, was to highlight that, although the effectiveness of an assignment against third parties would be determined by the proposed rule which favoured the habitual residence of the assignor, the "proprietary" effectiveness of the transaction between the assignor and assignee (and only those parties) would continue to be subject to the law governing their transaction.[39] Recital 38 remained despite the proposal's later removal.

15.28 In order to secure a first reading with the European Parliament on the Rome I Regulation it was agreed that a clause would be included to require a review to be undertaken by 17 June 2010 as to the effectiveness of assignations or subrogation of claims against third parties and the priority of the assigned or subrogated claim over a right of another person.[40] The British Institute of International and Comparative Law (BIICL) was commissioned to draft a report, which was completed in 2011.[41] The report proposes three

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[36] See paras 15.9–15.15 above.
[37] McParland, *The Rome I Regulation on the Law Applicable to Contractual Obligations* paras 18.67–18.104.
[38] British Institute of International and Comparative Law, *Study on the question of effectiveness of an assignment or subrogation of a claim against third parties and the priority of the assigned or subrogated claim over a right of another person* (2011) 151–152. See also F J Garcimartín Alférez, "The Rome I Regulation: Much ado about nothing?" 2008 The European Legal Forum (E) 78.
[39] F.J Garcimartin-Alférez, "Assignment of Claims in the Rome I Regulation: Article 14" in F Ferrari and S Leible (eds), *Rome I Regulation* (2009) 217 at 226. On third party effect generally, see also R Goode, "The Assignment of Pure Intangibles in the Conflict of Laws" in L Gullifer and S Vogenauer (eds), *English and European Perspectives on Contract and Commercial Law: Essays in Honour of Hugh Beale* (2014) 353 at 361.
[40] Art 27(2).
[41] British Institute of International and Comparative Law, *Study on the question of effectiveness of an assignment or subrogation of a claim against third parties and the priority of the assigned or subrogated claim over a right of another person: Final Report* (2011), available at http://ec.europa.eu/justice/civil/files/report_assignment_en.pdf.

potential connecting factors for determining the law which should govern the question of whether the assignation may be relied on against third parties, but does not favour one over the others. These are: (i) the law applicable to the contract between the assignor and assignee; (ii) the law applicable to the assigned claim; and (iii) the law of the assignor's habitual residence.[42] At the time of writing there appear to have been no further attempts to address this question.

Scottish practice

15.29 A report by the Scottish Executive Central Research Unit in 2002 on business finance for small and medium-sized businesses in Scotland showed that because of the limitations within Scottish law many businesses were being advised to prepare their contracts under English law.[43] The assumption among those interviewed for the report was that the decision in *Raiffeisen* is correct; it was therefore beneficial for Scottish businesses to use English equitable assignments rather than Scottish assignations as the former do not require notification in order to transfer title from the assignor to assignee.

15.30 However, the validity of this practice has been brought into question following the highly publicised Rangers Football Club administration.[44] In a discussion in relation to the applicability of the Rome Convention[45] Lord Hodge observed that the Convention was concerned only with the law applicable to contractual obligations and did not deal with proprietary rights:

> "I do not consider that the Rome Convention deals with proprietary rights at all. Article 1(1) states that the rules apply "to contractual obligations in any situation involving a choice between the laws of different countries". The creation of an equitable interest intermediate between a personal right and a right *in rem* is to my mind not a contractual obligation which the Convention covers."[46]

15.31 These comments were obiter.[47] They stand clearly in contrast with the *Raiffeisen* decision, as well as the Rome I Regulation which hold that such matters are within the scope of the Regulation, at least as far as the assignor and assignee are concerned.[48]

15.32 The position for Scottish businesses is therefore rather unclear. It could well be that any reform of the Rome I Regulation which saw an end to proprietary matters being treated as 'contractual' could cause issues for the multitude of small Scottish businesses which are currently engaged in the practice of assigning under English law. However, our recommendation to provide an option of either intimation or registration in order to complete an assignation under Scottish law would remove this potential problem.[49] The BIICL Report

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[42] See further Goode, "The Assignment of Pure Intangibles in the Conflict of Laws" at 366 ff.
[43] Scottish Executive Central Research Unit, *Business Finance and Security Over Moveable Property* (2002). See para 18.37 below.
[44] *Joint Administrators of Rangers Football Club Plc, Noters* 2012 SLT 599.
[45] The Rome I Regulation seems to have been overlooked.
[46] *Joint Administrators of Rangers Football Club Plc, Noters* 2012 SLT 599 at para 28. But See also *Akers (and others) v Samba Financial Group* [2017] UKSC 7 at paras 36 to 37 per Lord Mance.
[47] Counsel later withdrew his submission in relation to the Rome Convention and Contracts (Applicable Law) Act 1990.
[48] But as regards third party effect see McParland, *The Rome I Regulation on the Law Applicable to Contractual Obligations* para 18.52: "there was no legislative intention that Article 14(1) should be extended to cover the property aspects of any assignment (*erga omnes*)."
[49] See Chapter 5 above.

of 2011 made three proposals for reform, none of which involve treating proprietary matters as contractual issues.[50] The matter remains unresolved. It is therefore important that a solution is offered for Scottish businesses in the interim.

Jurisdiction

General

15.33 The term "jurisdiction" can be used in several different senses in legal discussion. For present purposes, the relevant sense is that a court has jurisdiction in proceedings where it has the authority to deal with the particular persons who are parties to the proceedings.[51] It is in this sense that the European Union has competence to legislate and determine the factors which connect parties or the dispute to courts of Member States. It is also in this sense that the rules of jurisdiction in intra-UK cases and those outwith the EU are found in the Civil Jurisdiction and Judgments Act 1982.[52] This is how jurisdiction is defined in this chapter. "Jurisdiction" can also be used in a second sense to describe when an action is within the power of a court and that a remedy can be competently granted by it. This type of jurisdiction may also be referred to as a court's *competence*.[53] Competence of a court to hear particular types of action is a matter for the domestic law of a legal system and does not involve international private law.

Application of jurisdictional rules

15.34 Generally speaking the Brussels I Regulation (Recast) applies where the defender in an action is domiciled in an EU Member State. The Regulation determines the courts of which Member States have jurisdiction. The Lugano Convention takes effect when the defender is domiciled in one of the three non-EU States which are parties to it, and similarly identifies the state or states whose courts have jurisdiction.

15.35 Where an action is a civil or commercial action within the meaning of the Regulation and the defender is domiciled in the UK, Schedule 4 to the 1982 Act allocates jurisdiction between the courts of the different legal systems within the UK.

15.36 Schedule 8 to the 1982 Act operates in determining whether the Scottish courts have jurisdiction in a wide range of civil proceedings not governed by the Brussels Regulation (Recast), the Lugano Convention or Schedule 4 to the 1982 Act. However Schedule 8 does not apply where a statute provides a rule of jurisdiction of a Scottish court on a specific subject-matter.[54] Accordingly a possible option in the present context is to disapply Schedule 8 by introducing a specific rule of jurisdiction.

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[50] See note 38 above.
[51] G Maher and B J Rodger, *Civil Jurisdiction in the Scottish Courts* (2010) para 1-01.
[52] Schedules 4 and 8.
[53] Maher and Rodger, *Civil Jurisdiction in the Scottish Courts* para 1-02.
[54] 1982 Act s 21(1). Furthermore, section 20(3) states that section 43 of the Courts Reform (Scotland) Act 2014 applies in respect of matters not governed by Schedule 8. This provision replicates an earlier version of section 20(3) concerning the interaction of Schedule 8 and section 6 of the Sheriff Courts (Scotland) Act 1907. It has been argued that section 6 of the 1907 Act had little, if any, application after the 1982 Act came into effect (Maher and Rodger, *Civil Jurisdiction in the Scottish Courts* paras 2-26–2-27) and the same is true of section 43 of the 2014 Act.

Grounds of jurisdiction

15.37 The next issue is the grounds of jurisdiction under each set of rules. Many of the grounds are the same in all sets.[55] These include the place of domicile of the defender;[56] the place of performance in contractual obligations;[57] prorogation of jurisdiction;[58] and multiple defender and third party proceedings.[59] Additionally Schedule 8 provides general grounds of jurisdiction. Of particular relevance to the present discussion are actions relating to rights in moveable property. Where such actions are governed by Schedule 8, the Scottish courts have jurisdiction where the property is located in Scotland.[60]

Discussion

15.38 The overall position is that, although Scotland retains competence to introduce rules for actions where the Brussels I Regulation (Recast) and the Lugano Convention do not apply, the current rules on jurisdiction are extensive and well settled. It is not clear to us that any reform is required here in the context of assignation of claims or indeed moveable transactions more generally.[61]

Conclusion

15.39 Reform of the rules of international private law as regards the applicable law in assignment (assignation) would generally have to be at a European level. But, for the UK the future applicability of EU rules following the withdrawal from the EU have yet to be worked out. It is clear that Article 14 of the Rome I Regulation is causing uncertainty and we would welcome clarification of the position of the applicable law as to the proprietary effects of assignments (assignations). It is also desirable that steps are taken to ensure consistency of choice of law rules, so as to avoid different results where the same issue is raised by different parties. Finally, the rules on jurisdiction are well-established at every level. We see no reason to depart from these rules.

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[55] The Lugano Convention and Schedule 4 to the 1982 Act are closely based on the original version of the Brussels I Regulation but do not take account of the revisions added by the Recast instrument. Many of the Schedule 8 grounds are based on the pre-recast Regulation but others have no counterpart in the other sets of rules.

[56] Brussels I (recast) Art 4; 1982 Act, Schedule 4, rule 1 and Schedule 8, rule 1; Lugano Convention Art 2.

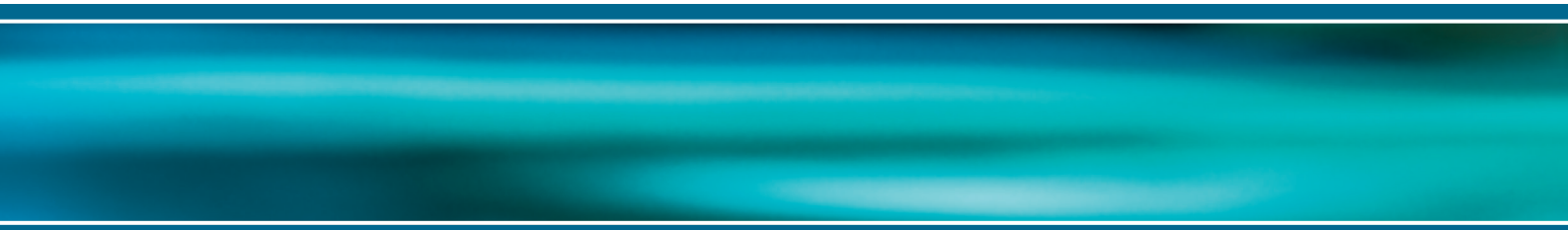
[57] Brussels I (recast) Art 7; 1982 Act, Schedule 4, rule 3 and Schedule 8, rule 2; Lugano Convention Art 5.

[58] Brussels I (recast) Art 25; 1982 Act, Schedule 4 rule 12 and Schedule 8, rule 6; Lugano Convention Art 23.

[59] Brussels I (recast) Art 8; 1982 Act, Schedule 4, rule 5 and Schedule 8, rule 2; Lugano Convention Art 6.

[60] 1982 Act, Schedule 8, rules 2 and 6.

[61] See para 39.13 below.



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promoting law reform

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Report on Moveable Transactions
Volume 2: Security over Moveable Property

report

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Report on Moveable Transactions Volume 2: Security over Moveable Property

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The Scottish Law Commission was set up by section 2 of the Law Commissions Act 1965 (as amended) for the purpose of promoting the reform of the law of Scotland. The Commissioners are:

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Contents

Chapter 16 Outline of the scheme

Introduction

16.1 This second volume of our Report on Moveable Transactions deals with reform of security over moveable property. In this chapter we provide an outline of the scheme which we recommend. In the Discussion Paper we did the same for the provisional scheme.[1] As for reform of the law of assignation of claims, there was considerable support in general for our proposals. We discuss this further below.[2] We do, however, highlight here the most important differences from the provisional scheme.

The scheme in practice

16.2 The scheme would enable secured lending to take place more easily and widely in Scotland. It would be possible for (a) security to be granted over corporeal moveable assets without having to deliver these to the creditor and (b) security to be granted over certain incorporeal moveable assets without having to transfer these to the creditor.

16.3 In Chapter 17 below we consider the current law in outline and the case for reform. As described in more detail in Chapter 18, the scheme amounts to a package of reforms to modernise the law of security over moveable property in Scotland so as to fulfil the needs of business today. Its underlying theme is that there should be more *options* available to those seeking to use their moveable assets for asset finance. Existing options such as possessory pledges and floating charges would be retained.

Targeted reform

16.4 As discussed also in Chapter 18, we have sought to learn lessons from previous attempts at reform which have failed. We have taken a targeted approach rather than recommending wholesale reform. The desire for commercial law to be broadly similar north and south of the Scotland/England border is accepted.[3] Thus there would be no radical rewriting of the law along a UCC–9/PPSA type model given the current lack of support for this among many working in this area in Scotland. "Recharacterisation", that is to say the compulsory conversion of quasi-security rights into actual security rights, would not be adopted. Nor would notice filing.

Statutory pledge: general

16.5 A new security right for moveable property would be introduced, called a "statutory pledge". This would be a "true" (or "proper") security: the grantee would acquire a subordinate right in security, with the provider of the security (normally the debtor) retaining

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[1] Discussion Paper, Chapter 3.
[2] See Chapter 18 below.
[3] On this subject more generally, see Lord Hodge, "Does Scotland need its own Commercial Law?" (2015) 19 EdinLR 299. Cf J Hardman, "Some Legal Determinants of External Finance in Scotland: A Response to Lord Hodge" (2017) 21 EdinLR 30.

title to the encumbered property. It would be the moveable property equivalent of the standard security over land.

16.6 The statutory pledge would be a "fixed" security. Thus the creditor's involvement would be needed to release property from it, in contrast with the floating charge. In the most significant departure from the scheme outlined in the Discussion Paper, there would not be a "floating" version of the statutory pledge or what might be called a "floating lien". Thus the statutory pledge would generally not be suitable for stock-in-trade where the provider of the security needs to be able to deal with the property freely. In that case the floating charge would continue to be used (assuming that the provider can grant a floating charge).

Statutory pledge: incorporeal moveable property

16.7 It would be competent to grant a statutory pledge over limited classes of incorporeal moveable property, namely financial instruments and intellectual property (IP). As a proper security right, various consequences would follow: (i) where the encumbered property generated an income stream (such as royalties from copyright), the stream would continue to be payable (unless and until default) to the provider of the security; (ii) the provider could grant more than one security right over the same asset, the security rights having priority according to the general law of ranking; and (iii) the provider could transfer the right to another party, subject always to the security right.

16.8 The limiting of the statutory pledge to financial instruments and IP is another important change from the scheme outlined in the Discussion Paper. There are several reasons for it: (a) these are the two types of incorporeal moveable property where the case for reform is most compelling; (b) permitting the statutory pledge over all incorporeal assets would have a more significant effect on unsecured creditors in an insolvency; (c) making statutory provision for fixed security over claims would be problematic without reform of insolvency law; and (d) the assignation in security would remain possible for all incorporeal assets so security can continue to be taken in that way. The statutory pledge could be granted over after-acquired financial instruments and IP, the security right not coming into existence until the provider acquired the property in question.

Statutory pledge: corporeal moveable property

16.9 It would also be competent to grant a statutory pledge over corporeal moveable property. This would be a non-possessory security. It would require registration. It could be granted over after-acquired property.

16.10 In certain cases buyers from the provider would take the property free of the statutory pledge. In particular we recommend that non-business acquirers of goods below a prescribed figure would be protected.

Asset types

16.11 Ships and aircraft would generally be excluded from the scope of the statutory pledge. But we think that the security right could be used for smaller vessels such as yachts which are not registered in the UK Ship Register. Apart from that, all corporeal moveable property, financial instruments and IP could be used as collateral in relation to the statutory pledge. This would of course be subject to issues of situation (*situs*) and to the general

proviso that the asset is one capable of being used as collateral. For example, non-transferable rights such as certain IP licences could not be used as collateral.

The attachment/perfection distinction

16.12 The attachment/perfection distinction to be found in UCC–9 and the PPSAs would not be adopted. Either a statutory pledge would be created and be effective against the world or it would not be. It could not be created as between the provider and the secured creditor, but not as regards third parties.

16.13 The statutory pledge would be a species of the genus "security" and thus would be subject to the general law of rights in security, both statutory and common law, except in so far as the legislation otherwise provided.

Ranking

16.14 The general principles of ranking would apply to the statutory pledge. A statutory pledge over a future asset could not take effect before the asset is actually acquired.

Ability to grant a statutory pledge

16.15 A statutory pledge could be granted by any person, not only companies.

Consumer protection

16.16 Private individuals not acting in the course of a business would be unable to grant a statutory pledge over after-acquired assets, unless they are granting the security to obtain the funds to purchase the asset.

16.17 They would also not be allowed to grant a statutory pledge over assets worth less than a prescribed figure. A court order would be necessary to enforce the security. There would also be protection for the relatively unusual situation where a statutory pledge is granted over someone's residence, such as a house boat.

Enforcement

16.18 In the case where businesses have granted statutory pledges, enforcement would be extra-judicial, in the interests of speed and keeping costs down. (But of course in some cases where there was a dispute about fact or law, litigation might be unavoidable.) Enforcement would usually result in sale of the asset. There would be other methods of enforcement, namely leasing or licensing of the encumbered property and appropriation of it.

Register of Statutory Pledges

16.19 There would be a new Register of Statutory Pledges ("RSP"), which would be comparable, in broad terms, with the registers used under UCC–9 and the PPSAs. The main difference would be that the statutory pledge document would be registered. The RSP would be public and electronic, and so searchable online. Registration would take place online.

16.20 The RSP would be used for the creation of statutory pledges. Where a statutory pledge is acquired by registration in the RSP, registration would be a necessary condition of

acquisition, rather than merely giving publicity to a right that had already been acquired. This differs from the notice filing approach under UCC–9 and the PPSAs. Where registration was in relation to after-acquired property, the statutory pledge could not be created until the property was acquired, which would be later than the date of registration. For example, company X grants a security over its vehicles present and future to Y and there is registration on 1 June. On 1 July X acquires ten new motor vehicles. The statutory pledge would encumber those vehicles on 1 July.

16.21 The RSP would be administered by the Keeper of the Registers of Scotland in the Department of the Registers and on the same financial basis as most other registers. It would, in general, be automated and require minimum intervention by the Keeper and her staff. The costs of the register would be covered by fees for registration, for searches etc. Thus, as with the Register of Assignations, there should be no cost to the taxpayer.

16.22 Registration would be by the name of the provider of the statutory pledge (normally the debtor), with possible exceptions, for example for motor vehicles where registration could perhaps be both by provider name and by Vehicle Identification Number (VIN). The rules would be fairly demanding as to the identity of the provider. For companies, not only company name and registered office address would be required, but also company number, because whereas names and addresses can change, the company number stays the same. For natural persons we recommend that date of birth should be required as well as name and address.

16.23 Registration would have third-party effect. But there would be defined exceptions where a third party would be unaffected. For example, someone buys goods unaware of a statutory pledge, because the entry for the pledge in the RSP has an inaccuracy which is seriously misleading. The registration is thus invalid and the buyer would obtain an unencumbered title.

16.24 In contrast to the scheme proposed in the Discussion Paper, registrations would remain on the RSP indefinitely, but there would be power for the Scottish Ministers to prescribe a lapse period for the statutory pledge if the RSP were to become cluttered. Decluttering would make the RSP easier to use.

16.25 It would be possible for misleading entries in the RSP to be corrected. The Keeper would have the power to remove those entries which had a manifest inaccuracy such as where there has been a frivolous or vexatious registration. Where an entry for a statutory pledge was redundant because the debt had been repaid, the provider of the security (normally the debtor) could demand that the secured creditor deletes the entry.

16.26 Registration would not be required for security in respect of financial instruments because of the Financial Collateral Arrangements (No. 2) Regulations 2003.[4]

Codification of the law of rights in security over moveable property

16.27 No attempt would be made to codify the law of rights in security over moveable property. But the possibility of future codification would remain.

[4] SI 2003/3226.

Treatment in insolvency

16.28 The statutory pledge would be a new type of "right in security" and would be subject to the general rules about rights in security to be found in insolvency legislation.

Floating charges

16.29 It would remain competent for companies etc. to grant floating charges.

16.30 Floating charges would continue to apply to land.

Possessory pledge

16.31 The law of possessory pledge would be the subject of certain important reforms: (i) the rules about forfeited pledges contained in the Consumer Credit Act 1974 would be reformed to make them fairer to debtors; (ii) the rule in *Hamilton v Western Bank*[5] would be overturned and pledge allowed by forms of delivery other than actual handing over to the pledgee;[6] and (iii) the remedies available for enforcement of a pledge outwith the context of the Consumer Credit Act 1974 would be broadened and be the same as for the statutory pledge. In a change to the scheme set out in the Discussion Paper we do not recommend registration for trust receipt financing. The possibility of further reform to possessory pledge in the future and codification would not be excluded.

International private law

16.32 No changes would be made to international private law. Existing international private law would continue to determine when substantive Scottish law would or would not apply. It may be that some reform to international private law would be desirable but that would be for the future. This too would be a difference from the approach of UCC–9 and the PPSAs, which generally include in the statute provisions regulating the international private law of moveable security.

How near to UCC–9 and the PPSAs?

16.33 The scheme outlined here would draw to some extent on the UCC–9/PPSA approach. The RSP would be broadly similar in relation to the information held, searching and the consequences of errors. But there would also be significant differences. Here are some features of the scheme that would be different from the UCC–9/PPSA approach:

(a) the absence of recharacterisation;

(b) there would be transactional filing rather than notice filing and a copy of the security document would be registered;

(c) there would be separate procedures for altering a register entry for juridical acts affecting the statutory pledge and for corrections of inaccuracies;

(d) the survival of the floating charge;

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[5] (1865) 19 D 152.
[6] On one view, Scots law has already implicitly abandoned the *Hamilton* rule. But this is by no means certain. See para 17.18 below.

(e) the absence of a set of rules about international private law; and

(f) the absence of a codification, or semi-codification, of secured transactions law in general.

Chapter 17 The current law and the case for reform

Introduction

17.1 In the Discussion Paper we outlined the current law in relation to security over corporeal moveable property, security over incorporeal moveable property and floating charges.[1] While it is unnecessary to restate that here, we do consider it essential to give a brief summary of these areas and the shortcomings of the present law which justify reform.

Security over incorporeal moveable property

(a) The current law

17.2 Security over property in Scotland can be classified as either "true" or "functional".[2] A "true" security right, also known as a "proper" security right, is where the provider of the security, normally the debtor, retains ownership of the property but grants the creditor what is known in property law as a "subordinate real right". A "real right" is a right in a particular piece of property. This is often explained as a right which is good against the world. Ownership is the principal real right. The other subordinate real rights include leases of land and servitudes (such as private rights of way) over land.[3]

17.3 Being a real right, a true right in security is effective against the provider's successors and in insolvency. For example, Stanley borrows £100 from a pawnbroker and in return pawns his watch. The pawnbroker obtains a real right in the watch, although Stanley remains owner. The effect of the real right is that if Stanley sold the watch to Triin, the pawnbroker's real right would remain and he could still enforce his security by selling the watch. Similarly, if Stanley became insolvent the watch could be sold and the £100 recovered in that way. Without the security over the watch, the pawnbroker would be left as an unsecured creditor with only his contractual claim against Stanley and be unlikely to recover the debt because of the insolvency.

17.4 In contrast, a "functional security" is where there is no subordinate real right in the property, but ownership is used for security purposes. For example, Glyn is selling a car to Hilda. In the contract of sale he stipulates that ownership is not to transfer until Hilda pays the total price, which they agree that she will pay in three instalments. Meanwhile she gets immediate possession of the car. In this situation, the retention of title clause is effectively acting as a security. And there is only one real right: the right of Glyn as owner. Hilda has no real right (until she pays the final instalment). This means that Glyn is protected if Hilda becomes insolvent as the car remains his.

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[1] Discussion Paper, Chapters 4, 6, 7 and 8. In addition, in Chapter 5 of the Discussion Paper we considered the nature of security rights.
[2] See eg Gretton and Steven, *Property, Trusts and Succession* paras 21.11–21.15.
[3] See generally Reid, *Property* paras 3–5 and Gretton and Steven, *Property, Trusts and Succession* ch 2.

17.5 Cars (and indeed watches) of course are *corporeal* moveable property. Our concern here is *incorporeal* moveable property. Under the current law a true security is apparently *not* possible. The exception is the floating charge, but its exact nature is unclear and probably does not become a subordinate real right until enforcement.[4] Therefore, aside from the floating charge, security can only be obtained over incorporeal moveable property by *transferring* it to the creditor. This is usually done by means of an assignation in security, and being a form of assignation, the general law of assignation applies.

17.6 Most incorporeal moveable property consists of claims. As discussed earlier in this Report,[5] a claim is the right of one person against another person to have an obligation performed. Typically the obligation is to pay money. For a claim to be assigned in security, the general rules of the law of assignation apply. This means that under the current law there must be intimation to the debtor. The recommendations which we made earlier in relation to assignation would allow registration to be used instead.[6]

17.7 Two types of incorporeal moveable property deserve particular mention in the context of security and the recommendations to be made later.[7] The first is intellectual property. Assignation usually involves three parties. Thus in the transfer of a monetary claim, there are the original creditor, the new creditor, and the debtor. Intellectual property is incorporeal moveable property, but its assignation involves two parties only, not three: only an assignor and an assignee (But there may be implications for third parties, as where a copyright has been licensed by X to Y, and thereafter X assigns the copyright itself to Z.)

17.8 Despite this difference, assignation remains the only way in Scotland to use intellectual property for security purposes (apart from the floating charge). For example, if Paul holds copyright in a book and wishes to use that copyright as collateral for a loan from Ruth, that can be done, but only by way of an assignation in security, so that the copyright is transferred to Ruth, subject to Paul's personal right against Ruth for a re-transfer if and when the loan is repaid. A real-life example involves Rangers Football Club, which in April 2015, was reported to have granted security over its trade marks by means of assignation.[8]

17.9 Intellectual property is regulated by UK legislation. Registered intellectual property such as patents are registered in UK registers. This raises the issue of the circumstances in which Scottish or English law applies in relation to creating security. As discussed below in Chapter 39, in general terms the law that governs a security right is the law of the place where the property in question is situated: the *lex situs* (the *lex rei sitae*). The predominant view seems to be that the law applicable to security over intellectual property depends on the *situs* of the property and that the *situs* of intellectual property, as between England and Scotland, is determined by the domicile of the holder of the property.[9]

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[4] *National Commercial Bank of Scotland Ltd v Liquidators of Telford Grier Mackay & Co Ltd* 1969 SC 181 at 184. For a full discussion see A D J MacPherson, *The Attachment of the Floating Charge in Scots Law* (PhD Thesis, University of Edinburgh, 2017) especially chapters 2 and 5. English law also finds the nature of the pre-crystallised floating charge problematic: see for instance S Worthington, "Floating Charges: The Use and Abuse of Doctrinal Analysis" in J Getzler and J Payne (eds), *Company Charges: Spectrum and Beyond* (2006).

[5] See paras 4.12–4.16 above.

[6] See Chapter 5 above.

[7] See Chapter 22 below.

[8] See http://www.bbc.co.uk/sport/0/football/32280000.

[9] "An English patent is a species of English property of the nature of a chose in action and peculiar in character" says Lord Evershed in *British Nylon Spinners Ltd v Imperial Chemical Industries Ltd* [1953] Ch 19 at 26. This

17.10 The Registered Designs Act 1949, the Patents Act 1977 and the Trade Marks Act 1994 have provisions on the registration of security rights over the intellectual property which they govern.[10] As we noted in the Discussion Paper,[11] these provisions are not entirely clear and we say more about them below, in Chapter 22.

17.11 The second type of incorporeal moveable property which deserves particular mention is financial instruments, such as company shares and bonds. Security here is achieved by the provider transferring the property to the creditor. In the case of shares and bonds the creditor then requires to be registered by the company as holder.[12] The transferee's right is constituted by registration,[13] so that a mere agreement is insufficient. Thus in Scottish law no equivalent to the English fixed equitable charge is available.[14]

(b) The case for reform

17.12 The absence of a true right in security over incorporeal moveable property is a very unsatisfactory feature of Scottish moveable transactions law.[15] It means that security can only be achieved by transfer. The nature of a transfer is that it can only be done once. If Brian assigns in security to Carol his patent for an invention, Brian cannot (other than fraudulently) assign the patent again to Edward. Multiple security rights are not possible. Following the assignation to Carol, all Brian could offer as security is his contingent right against Carol to a re-assignation of the patent, which is cumbersome to achieve.

17.13 A further problem with transfer is the risk to the provider if the creditor becomes insolvent. Thus if Michalina transfers financial instruments such as shares in a company in security to Anne and Anne is sequestrated, what is Michalina's position? Can Anne's trustee in sequestration simply sell the instruments? It may be that he cannot because the law would imply a trust in favour of Michalina,[16] but the position is by no means certain.

17.14 Moreover, debtors may not wish to sign over ownership of their shares. Although such a transfer will not usually mean that the transferee becomes a holding company of the share issuer, arrangements have to be made to make sure that, except if there is default on the secured debt, voting rights can be exercised by the transferor. Dividends and communications from the issuing company also have to be transmitted. There are also complications arising from the legislation which came into force on 1 April 2016 which requires companies and LLPs to have a Person of Significant Control (PSC) Register. These are discussed below.[17] With intellectual property it is necessary to enter into cumbersome arrangements to enable the provider to be able to continue to deal with the property.[18]

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seems the right approach. Likewise one could say that "a Scottish patent is a species of Scottish property of the nature of incorporeal moveable property and peculiar in character."

[10] Registered Designs Act 1949 s 19; Patents Act 1977 s 33; and Trade Marks Act 1994 ss 24 and 25.

[11] Discussion Paper, paras 7.22–7.27.

[12] Except in the case of bearer shares or bearer bonds. But these are to disappear in terms of the Small Business, Enterprise and Employment Act 2015 s 84.

[13] Cf *Morrison v Harrison* (1876) 3 R 406.

[14] See *Farstad Supply A/S v Enviroco Ltd* [2011] UKSC 16 at para 4 per Lord Collins of Mapesbury.

[15] Discussion Paper, paras 18.4–18.8.

[16] Cf *Purnell v Shannon* (1894) 22 R 74.

[17] See paras 22.26–22.27 below.

[18] See eg A Orr and T Guthrie, "Fixed Security Rights Over Intellectual Property in Scotland" [1996] 18 European Intellectual Property Review 596.

17.15 The current state of the law can be seen to have serious consequences in practice. In an article published in 2017, Jonathan Hardman, an associate at Dickson Minto WS, recollects:

> "an informal conversation with a London counterparty on a debt finance transaction in which the counterparty indicated that certain of his international bank clients were unwilling to allow their corporate borrowers a blanket permission to incorporate new Scottish subsidiaries on the grounds that taking fixed securities over their shares was too difficult – but that blanket permissions for the incorporation of English companies and Channel Island companies would pose no issue."[19]

17.16 Ultimately the problems identified in this section follow from the fact that assignation in security gives the creditor *too much*. It is a title transfer, which is not actually what the parties want. Ingenuity must be used to try to undo some of the consequences of that transfer, but the results are never entirely satisfactory. Since assignation in security is merely a form of assignation, it also suffers from the general defects of the law of assignation.

Security over corporeal moveable property

(a) The current law

17.17 The principal express security right over corporeal moveable property in Scottish law is pledge.[20] Pledge is an ancient security, which is recognised in almost all legal systems.[21] The provider ("pledger") retains ownership of property and the secured creditor ("pledgee") acquires a subordinate real right in it.

17.18 Pledge requires the delivery of the property from the pledger to the pledgee. In other words, the creditor requires to be placed in possession.[22] The general law recognises various forms of delivery.[23] First, there is *actual* delivery, where the property is physically handed over or the pledgee is given physical control of the property.[24] Secondly, there is *constructive* delivery. The main example of this is where the property is held by a third party custodier, such as a warehouse. Delivery is effected by instructing the custodier to hold to the order of the creditor. Thirdly, there is *symbolical* delivery, which appears to be restricted to bills of lading in relation to goods being shipped. Possession of the goods can be transferred by handing over the bill of lading. Intimation to the shipping company is unnecessary. According to the case of *Hamilton v Western Bank*[25] pledge requires actual delivery to the pledgee. While the decision has been the subject of contrary subsequent authority[26] and trenchant academic criticism,[27] it has never been formally overruled.

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[19] J Hardman, "Some Legal Determinants of External Finance in Scotland: A Response to Lord Hodge" (2017) 21 EdinLR 30 at 31.
[20] As an express security, it contrasts with tacit securities, such as lien or the landlord's hypothec, which arise by operation of law.
[21] See Steven, *Pledge and Lien* paras 3-01–3-02.
[22] See generally C Anderson, *Possession of Corporeal Moveables* (2015).
[23] See generally, Reid, *Property* paras 619–623 (W M Gordon) and Carey Miller with Irvine, *Corporeal Moveables* paras 8.12–8.27.
[24] For example, by being given the keys of a car.
[25] (1856) 19 D 152.
[26] *North Western Bank, Limited v John Poynter, Son & Macdonalds* (1894) 22 R (HL) 1, [1895] AC 56.
[27] A F Rodger, "Pledge of Bills of Lading in Scots Law" 1971 Juridical Review 193; G L Gretton, "Pledge, Bills of Lading, Trusts and Property Law" 1990 Juridical Review 23; and Steven, *Pledge and Lien* ch 8.

17.19 Where a private individual pledges assets to a professional pledge-taker, the transaction is known as "pawn" and the creditor as a "pawnbroker". Pawnbroking is regulated by the Consumer Credit Act 1974.[28] The rules on enforcement of pledges (except for pawn where the 1974 Act governs matters) are found in the common law and are relatively restrictive. Thus in the absence of a contractual power of sale in the pledge contract, the pledgee requires to go to court.[29]

17.20 The floating charge can cover corporeal moveable property, but can only be granted by certain corporate bodies. We discuss it below. There are also available aircraft mortgages[30] and ship mortgages, but these are clearly limited in scope to the types of assets with which they are synonymous.[31]

17.21 The restrictive nature of true security rights over corporeal moveables has resulted in considerable use of functional securities, where ownership of property functionally acts as a security. As we noted above, it is common for sellers of goods to retain ownership until the price, or indeed all sums[32] owed to them by the buyer, is/are paid. If the buyer becomes insolvent the seller can retrieve the goods. Hire-purchase (HP) works in a similar way to retention of title, but often involves three parties: a supplier sells the goods to a financing company, which then enters into a HP contract with the customer. The relationship between the financing company and the customer is one of hire, but with a purchase option. But once again the key aspect is that there is protection for the creditor (the financing company) in the event of the insolvency of the debtor (the customer).

17.22 Another form of functional security is transfer to the creditor with retention of possession. The financed party can sell the goods to the financing party, retaining possession on the basis of another contract. For example, the other contract could be a finance lease, or operating lease, or HP. Or it could be a sale back, subject to retention of title. In all cases the financing party has, as a result of the original sale, ownership of the goods, and so is protected against the risk of insolvency.

17.23 But such arrangements are subject to a problem. Section 62(4) of the Sale of Goods Act 1979 provides that "the provisions of this Act about contracts of sale do not apply to a transaction in the form of a contract of sale which is intended to operate by way of mortgage, pledge, charge, or other security." That means that, like other transfers to which the 1979 Act does not apply, such as donations, the common law applies, with the result that delivery is necessary for ownership to pass.[33] Much depends on how the expression "intended to operate by way of mortgage, pledge, charge, or other security" is interpreted. A sale at fair value, followed by a lease on ordinary commercial terms, would be unaffected by the provision. At the other extreme, the provision would strike at a sale at undervalue[34] coupled

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[28] Consumer Credit Act 1974 ss 114–122.
[29] Steven, *Pledge and Lien* paras 8-04–8-10.
[30] As well as international interests in aircraft objects under the Cape Town Convention. See Chapter 21 below.
[31] See Chapter 21 below.
[32] *Armour v Thyssen Edelstahlwerke AG* 1990 SLT 891, [1991] 2 AC 339.
[33] The common law, following Roman law, requires delivery for the transfer of the ownership of corporeal moveable property. The common law continues to apply in so far as not ousted by statute. For a review of section 62(4) (and its predecessor, section 61 of the Sale of Goods Act 1893) and the relevant case law, see G L Gretton, "The Concept of Security" in D J Cusine (ed), *A Scots Conveyancing Miscellany: Essays in Honour of Professor J M Halliday* (1987) 135–138. See also Carey Miller with Irvine, *Corporeal Moveables* ch 11. Cf S Styles, "Debtor-to-Creditor Sales and the Sale of Goods Act" 1995 Juridical Review 365.
[34] The reason for the undervalue is that typically a lender will expect "collateral margin" ie that the value of the collateral should exceed the amount of the loan. That provides a margin of safety.

with a contract binding the seller to buy back. But there are cases in between where it is uncertain how the law would be applied. The 1979 Act does not define "security".

17.24 As section 62(4) does not invalidate the transactions to which it refers, but merely disapplies the Act to them, leaving them to the common law, what sometimes happens is that the goods are delivered to the financing party and immediately re-delivered.[35] Whether arrangements such as these work is not certain. It might be argued that the delivery is too transient to be regarded as valid.

(b) The case for reform

17.25 The requirement for delivery in pledge makes it an unsatisfactory security right commercially. For it is impossible for a business to function if its creditor has possession of its corporeal moveable assets such as its office furniture, computers and vehicles.[36] This is something recognised now by many jurisdictions and has resulted in law reform to introduce non-possessory securities constituted by registration.[37] Even where the context is a consumer rather than a business one, pledge has its disadvantages. Art-secured lending is increasing in importance worldwide and non-possessory security, where owners "are still able to enjoy their Dan Flavin or Andy Warhol at home or in the gallery",[38] is favoured. In Scotland the painting has to be handed to a pawnbroker.

17.26 While pledge can be a convenient security where goods such as whisky are stored in a warehouse, or goods being shipped are represented by a bill of lading, the decision in *Hamilton v Western Bank* casts an unwelcome shadow of doubt over such transactions. For example, it was reported in 2016 that a £20 million wine collection stored in a warehouse in Wiltshire was pledged by a businessman to obtain loan funding for a new venture.[39] *Hamilton* may deter such a transaction in Scotland. The relatively restrictive nature of our common law in relation to enforcement of pledges is also not suitable for the needs of modern commerce.

17.27 As has been seen, the limitations of pledge have resulted in the use of functional securities. But these too have their drawbacks. Transferring ownership of goods to a creditor while retaining possession may be ineffective because of section 62(4) of the Sale of Goods Act 1979. Hire-purchase is a relatively complex arrangement, typically involving three parties. In addition, it is only available for acquisition finance. It is no good for someone who already owns an asset such as a car and who wants to raise finance against it. In contrast in England and Wales, bills of sale can be used. Although that area of law has unsatisfactory features which have led to the Law Commission for England and Wales

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[35] See the example given in the Discussion Paper, para 6.41.

[36] See eg Hamwijk, *Publicity in Secured Transactions Law* 2–3; A Morell and F Helsen, "The Interrelation of Transparency and Availability of Collateral: German and Belgian Laws of Non-possessory Security Interests" (2014) 22 European Review of Private Law 393 at 398; and Calnan, *Taking Security* para 2.04.

[37] See eg Hamwijk, *Publicity in Secured Transactions Law* 7–10 and Gullifer and Akseli (eds), *Secured Transactions Law Reform.*

[38] Deloitte Art and Finance Report (5th edn, 2017) p 163 available at https://www2.deloitte.com/content/dam/Deloitte/lu/Documents/financial-services/artandfinance/lu-art-finance-report.pdf.

[39] *The Times* 30 December 2016 (online edition).

recommending its replacement with a new Goods Mortgages Act,[40] once again this demonstrates a gap in Scottish law.

17.28 Under the current law there are situations in which creditors have no alternative if they wish security other than to hold title to goods such as vehicles. They then have to be liable for the administrative and legal consequences when all they actually wish is a true security right. The point made above in relation to security over incorporeal moveable property holds true here too. Functional security gives the creditor too much. The law requires to be reformed to enable true security.

Floating charges and agricultural charges

(a) The current law

17.29 Floating charges merit their own treatment, because these cover both corporeal and incorporeal property, and indeed both moveable property and land. Originally a product of English equity, they were introduced to Scotland by the Companies (Floating Charges) (Scotland) Act 1961. This implemented the Eighth Report of the Law Reform Committee for Scotland.[41] The main reason for the introduction of the floating charge was the restrictive nature of the common law in relation to security over moveable property.

17.30 As has been mentioned, only certain entities can grant floating charges, in particular companies,[42] limited liability partnerships[43] and, since 2015, building societies.[44] Usually floating charges are granted over all the entity's assets, but it is also possible to have a "limited asset" floating charge over a particular asset or categories of asset.[45]

17.31 The way in which a floating charge works is that assets acquired by the entity automatically fall under the charge and assets disposed of are automatically freed from the charge. So long as the company stays in business, the charge continues to "float" in the manner described, and so long as the "floating" continues the effect of the charge is very limited. This contrasts in English law with a "fixed" charge which "sticks" to the property meaning that the company is not free to deal with it. But a floating charge can cease to float. When it ceases to float it "crystallises" or (synonymously) "attaches". The former term is used in England, and in practice in Scotland too, but the Scottish legislation uses only the latter term.

17.32 The legislation provides that when a floating charge "attaches" it takes effect as if it were a "fixed" security.[46] Thus for land it arguably becomes a deemed standard security, for a claim it becomes a notionally intimated assignation, and so on. Attachment can happen in

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[40] See Law Commission, Bills of Sale (Law Com No 369, 2016). It was announced in the Queen's Speech that a Goods Mortgages Bill would be introduced as part of the UK Government's legislative programme. See http://www.lawcom.gov.uk/project/bills-of-sale/.

[41] Cmnd 1017 (1960). See R B Jack, "The Coming of the Floating Charge to Scotland: an Account and an Assessment" in D J Cusine (ed), *A Scots Conveyancing Miscellany: Essays in Honour of Professor J M Halliday* (1987) 33.

[42] Companies Act 1985 ss 462–464.

[43] Limited Liability Partnerships Regulations 2001 (SI 2001/1090) reg 4 and Sch 2.

[44] Financial Services (Banking Reform) Act 2013, Sch 9. See the Financial Services (Banking Reform) Act 2013 (Commencement (No. 8) and Consequential Provisions) Order 2015 (SI 2015/428).

[45] See eg H Patrick, "Receivership of Foreign Based Companies" 2010 SLT (News) 177.

[46] Companies Act 1985 s 463; Insolvency Act 1986 s 53(7); and (prospectively) Bankruptcy and Diligence etc. (Scotland) Act 2007 s 47. For a comprehensive analysis see A D J MacPherson, *The Attachment of the Floating Charge in Scots Law* (PhD Thesis, University of Edinburgh, 2017).

three ways: liquidation (winding up), administration and receivership.[47] However, as a result of the Enterprise Act 2002, floating charges granted after 5 September 2003 are generally not enforceable by receivership. But there are numerous exceptions,[48] so that the overall picture is highly complex.

17.33 Floating charges granted by companies must normally be registered in the Companies Register under the rules discussed in Chapter 36.

17.34 Finally, mention should be made of agricultural charges. These were introduced by the Agricultural Credits (Scotland) Act 1929, in the wake of similar legislation for England and Wales, namely the Agricultural Credits Act 1928. The 1929 Act enables agricultural co-operatives to grant a floating non-possessory security to a bank.[49] The effect is similar to a floating charge, though one important difference is that whereas a floating charge can cover property of every type, the agricultural charge is limited to "stocks of merchandise".[50] Under the legislation as passed, agricultural charges had to be registered.[51] This requirement was repealed by the Financial Services and Markets Act 2000 (Consequential Amendments and Repeals) Order 2001.[52] Nowadays agricultural charges are rarely used in practice.

(b) The case for reform

17.35 While welcomed by financial institutions, floating charges have not fitted in very well with the general principles of Scottish law.[53] Floating charges are creatures of equity and our law does not have the law-and-equity divide recognised south of the border. The result has been many conceptual difficulties, culminating in the landmark House of Lords decision in *Sharp v Thomson*,[54] which threatened to undermine the very foundations of Scottish property law.[55] This led to extensive academic criticism.[56] In 2017 in the Inner House case of *MacMillan v T Leith Developments Ltd (in receivership and liquidation)*[57] Lord Drummond Young said:

> "The introduction of the floating charge into Scots law, and subsequently the concept of receivership, have created significant practical problems. A large part of the difficulty has, I think, been an attempt to reproduce concepts of English equity in a system that has no similar institution. The conceptual structure of English equity is distinctive, being based, in its original form, on a series of general principles that can be adapted to produce justice in individual cases. It is difficult to translate the

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[47] But it is less common in the case of administration. See D Cabrelli, "The curious case of the 'unreal' floating charge" 2005 SLT (News) 127.
[48] The 2002 Act did not disallow receivers, but only administrative receivers. For the definition of these see the Insolvency Act 1986 s 251. For the numerous exceptions see s 72B ff of that Act. The resulting situation is a mess.
[49] 1929 Act s 5. For the definition of "bank" for this purpose, see the Financial Services and Markets Act 2000 (Consequential Amendments and Repeals) Order 2001 (SI 2001/3649) art 217.
[50] 1929 Act s 5.
[51] 1929 Act s 8.
[52] SI 2001/3649 art 216.
[53] In the leading English case of *National Westminster Bank plc v Spectrum Plus Ltd* [2005] UKHL 41 at para 50 Lord Hope of Craighead describes the floating charge as a "cuckoo in the nest of Scots property law".
[54] 1997 SC (HL) 66. The case involved the transfer of land. In the subsequent case of *Burnett's Tr v Grainger* 2004 SC (HL) 19 the House of Lords rowed back, but in the meantime the matter had been referred to this Commission. See Scottish Law Commission, Report on *Sharp v Thomson* (Scot Law Com No 208, 2007).
[55] See eg K G C Reid, "Equity Triumphant: *Sharp v Thomson*" (1997) 4 EdinLR 464.
[56] See eg D Cabrelli, "The Case against the Floating Charge in Scotland" (2005) 8 EdinLR 407. And see also A D J MacPherson, "A Vicious Circle: The Ranking of Floating Charges and Fixed Securities" 2014 Edinburgh Student Law Review 67.
[57] [2017] CSIH 23.

institutions of English equity into another legal system, especially one based on the more rigorous conceptual structure of Roman law, as is the case with Scots law and most other European legal systems other than English law."[58]

17.36 Floating charges were the subject of a previous review by this Commission, which resulted in the passing of Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007. It has never been brought into force. The reason for that is discussed in the next chapter. Our focus here is why the floating charge is inadequate by itself to meet the needs of modern business.

17.37 The fact that floating charges can only be granted by certain entities means that there is a significant gap in moveable transactions law in relation to private individuals and bodies which cannot grant a floating charge, such as sole traders, partnerships and limited partnerships. We do not recommend the extension of the floating charge to these other persons, given the difficulties and inadequacies of floating charges law.

17.38 Floating charges also contrast unfavourably with "fixed" securities such as pledge for various reasons, notably:

(a) A floating charge, unlike a fixed security, is subject to the claims of the preferential creditors.[59]

(b) A floating charge, unlike a fixed security, is subject to the "prescribed part".[60] This is a sum of money taken from the floating charge-holder and made available to the unsecured creditors.

(c) A floating charge, unlike other security rights, is subject to the expenses of an administration.[61]

(d) An administrator's power to deal with property subject to a floating charge is more extensive than in the case of other types of security right.[62]

(e) The debtor can alienate the charged assets, in such a way as to remove them from the scope of the charge, without the charge-holder's consent. That is not the case with a fixed security.[63]

(f) "Effectually executed diligence" carried out by other creditors before attachment does not trump a fixed security but does trump a floating charge.[64]

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[58] [2017] CSIH 23 at para 121.
[59] Insolvency Act 1986 s 40 (receivership); Insolvency Act 1986 s 175 (liquidation); Insolvency Act 1986 Sch B1 para 65 (administration).
[60] Insolvency Act 1986 s 176A. For discussion, see *QMD Hotels Ltd Administrators, Noters* [2010] CSOH 168, 2011 GWD 1–42.
[61] Insolvency Act 1986 Sch B1 para 99(3). (*Re Nortel GmbH* [2010] EWHC 3010, [2011] Pens LR 37 illustrates the significance of this rule.) In England and Wales the same is true of liquidation expenses: Insolvency Act 1986 s 176ZA.
[62] Insolvency Act 1986 Sch B1 para 70.
[63] In English law an exception would be where there is a fixed equitable charge and there is a buyer who takes without notice.
[64] Companies Act 1985 s 463; Insolvency Act 1986 ss 55 and 60. The precise meaning of this rule is not entirely clear and has been the subject of much litigation. See *Lord Advocate v Royal Bank of Scotland* 1977 SC 155 overruled by *MacMillan v T Leith Developments Ltd (in receivership and liquidation)* [2017] CSIH 23. See also S

17.39 It is apparent from this list that there are many advantages of fixed security over floating charges. But in Scotland effectively the only fixed security offered by the current law over moveable property is pledge. Hence the need for a new fixed security.

17.40 In relation to agricultural charges we consider that there is a strong case for these ceasing to be competent given their lack of use in practice, the lack of the need for registration and the fact that floating charges are normally used instead.[65]

Economic case for reform

17.41 The economic justification for our recommendations is set out in the Business and Regulatory Impact Assessment (BRIA), which is available on our website and is summarised in Chapter 1.

Comparative case for reform

17.42 This chapter has shown that most of the current Scottish law on security over moveable property is non-statute law. The ability for the courts to innovate is limited; change brought about by case law is inevitably modest and incremental.[66] Today's law of pledge would be readily recognisable to the Scots lawyer of the time of Viscount Stair in the late seventeenth century.[67] The last significant statutory innovation was the introduction of the floating charge in 1961. As we noted in Chapter 1, the last twenty years have seen significant statutory reforms in other comparable jurisdictions, such as Australia, Jersey, New Zealand and Belgium,[68] and the publication of several transnational instruments, such as the DCFR and the UNCITRAL Model Law on Secured Transactions. When one considers all of these developments, coupled with the current pressure to reform the law of England and Wales,[69] it is clear that without significant change, Scottish secured transactions law is going to become even further out of touch with modern international standards.

Wortley, "Squaring the circle: revisiting the receiver and 'effectually executed diligence'" 2000 Juridical Review 325.

[65] See Chapter 38 below.

[66] Lord Rodger of Earlsferry, "Judges and academics in the United Kingdom" (2010) 29 University of Queensland LJ 29 at 32, quoted in K G C Reid, "Smoothing the Rugged Parts of the Passage: Scots Law and its Edinburgh Chair" (2014) 18 EdinLR 315 at 338.

[67] See A J M Steven, "Rights in Security over Moveables" in K Reid and R Zimmermann (eds), *A History of Private Law in Scotland* , vol 1 (2000) 333 at 341.

[68] There were also significant changes made to French law in 2006. See the French Civil Code arts 2333 ff.

[69] See para 1.32 above.

Chapter 18 The approach to reform

Introduction

18.1 In this chapter we begin by reviewing briefly the previous unsuccessful attempts to reform secured transactions law in Scotland and also in the United Kingdom generally. We discuss the apparent reasons for this lack of success. We then set out the approach which we have decided to take and explain why we have chosen not to pursue a functionalist approach as exemplified by the Uniform Commercial Code article 9 (UCC–9) and the Personal Property Security Acts (PPSAs).

18.2 Chapter 10 of the Discussion Paper considered in some detail previous reviews of the law and therefore we require only to give a briefer account here.[1] For the most part we leave the issue of company charges registration to Chapter 36 below.

Summary of the UCC–9 and PPSA approach

18.3 The Crowther Report, the Halliday Report and the Diamond Report[2] all recommended the adoption of a UCC–9/PPSA-type system. Before looking at these, it is necessary to provide a short summary of that approach here, as without this it is difficult to appreciate the level of change which these reports recommended. In Chapter 13 of the Discussion Paper a much fuller account is given.[3]

18.4 The UCC is a model law, the original version of which was published in 1952 and subsequently adopted by the various US states.[4] Article 9 deals with secured transactions in relation to moveable property. One of the key impetuses for reform was that US law did not recognise the floating charge.[5] UCC–9 in turn strongly influenced the PPSAs, beginning in the Canadian provinces and now also to be found in many other jurisdictions, such as New Zealand, Australia and Papua New Guinea.[6]

18.5 The first and most important feature of UCC–9 and the PPSAs is that they take a functional approach to security rights.[7] Transactions which function as security rights, even although they are not formally security rights (that is to say not true rights in security[8]), are treated as security rights. So, for example, retention of title and hire-purchase are regarded as security rights, as are assignations in security. A trust set up for the purposes of security is also so treated. The consequence of this is that these transactions have to obey the rules of the system, in particular there must be registration in order for there to be priority against

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[1] See also Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* ch 23.
[2] For these, see paras 18.9–18.17 below.
[3] See also H Beale, "An Outline of a Typical PPSA Scheme" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 7–19.
[4] See further P Winship, "An Historical Overview of UCC Article 9" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 21–48.
[5] *Benedict v Ratner* 268 US 353 (1925). This was a New York decision, but accepted in other States too. For the pre-UCC law see G Gilmore, *Security Interests in Personal Property* (1965).
[6] See generally Gullifer and Akseli (eds), *Secured Transactions Law Reform*.
[7] See eg Cuming, Walsh and Wood, *Personal Property Security Law* ch 2.
[8] See paras 17.21–17.24 above.

third parties, such as another creditor who takes security subsequently. This statement is subject to some qualifications. For example, in New Zealand security interests are effective in insolvency without registration.[9] And, generally under UCC–9 and the PPSAs, possession of the asset by the creditor is an alternative means of perfection.[10]

18.6 Secondly, the UCC–9/PPSA approach to registration is very different to what Scottish lawyers are currently familiar with, for example for standard securities in relation to land. The system of registration is called "notice filing". The document granting the security is not registered. What is registered is a second document, called a "financing statement". It contains only the barest information;[11] normally the details of the security provider and the creditor and the asset category identified from a tick-box list. The registration can happen before or after the security is granted. And the same registration can cover several security interests.[12] Notice filing nowadays normally happens electronically and essentially all the registrar does is maintain the register. Financing statements are not checked by the registrar, in contrast, for example, to the position in the UK when charges (security rights) are registered in the Companies Register.

18.7 Thirdly, UCC–9 and the PPSAs recognise a fundamental distinction between "attachment" and "perfection". A security interest is said to have "attached" when it can be enforced by the secured creditor against the provider of the security[13] and "perfected" when it gains priority against third parties.[14] Although perfection can be explained broadly in terms of third party effect, under UCC–9 and the PPSAs mere attachment can in some cases have such effect. Under UCC–9 an attached but unperfected security interest is, it seems, effective against a donee, and also against a buyer who (a) is not in good faith and (b) is not a buyer in the ordinary course of business.[15] And in New Zealand, as noted above, unperfected (unregistered) security interests are effective in insolvency without registration, but not against secured creditors who have registered, or against purchasers. To Scottish lawyers at least the idea of a security interest that does not have priority against third parties is an odd one. The point of a security right lies in having priority, particularly in insolvency. Having said that, the idea of an attached but unperfected security interest has sense. The creditor can use the enforcement methods appropriate to that security, as an alternative to diligence, and that may be an attractive option. For example, diligence can be slow. Moreover, as we have seen, attachment confers on an unperfected security interest a limited degree of third party effect. Be that as it may, the attachment/perfection distinction contrasts with the traditional Scottish approach that a security is either effective or it is not.[16]

18.8 Fourthly, under the UCC–9 and the PPSAs transactions such as assignation in security, retention of title in sale, hire-purchase, and certain moveable leases, are

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[9] On which, see M Gedye, "The Development of New Zealand's Secured Transactions Jurisprudence" 2011 University of New South Wales Law Journal 696 at 702–703.
[10] And in respect of certain financial assets another possibility may be "control". See Beale (n 3) at 13.
[11] A standard work calls it the "bikini" of the UCC: J J White and R S Summers, *Uniform Commercial Code* (5th edn, 2000) para 22-10.
[12] The term "interest" is generally used rather than "right".
[13] UCC § 9–203(a): "A security interest attaches to collateral when it becomes enforceable against the debtor with respect to the collateral." There can be a concluded security agreement without attachment, for attachment calls for certain requirements over and above agreement. These requirements are set out in UCC § 9–203.
[14] The UCC does not seem to state this expressly, but this is the point of the concept.
[15] This limited effect of an unperfected security interest emerges from UCC § 9–317(b) read with UCC § 9–330. On this point see H Sigman, "Perfection and Priority of Security Rights" in H Eidenmüller and E-M Kieninger (eds), *The Future of Secured Credit in Europe* (2008) 143 at 147.
[16] See eg *Bank of Scotland v Liquidators of Hutchison Main & Co* 1914 SC (HL) 1.

"recharacterised", that is to say regarded as being a transfer of title subject to a reservation of a security interest. This is a complex subject and best demonstrated by an example. Ruth Ltd grants a security to the Saltire Bank over both its present and after-acquired assets. And suppose that later Tom sells goods to Ruth Ltd on credit terms, reserving title (ownership) until payment. Under current Scottish law, the bank's security would be a floating charge, and Tom would be protected because the effect of the retention of title would be that the goods would not belong to Ruth Ltd until they have been paid for. But the effect of recharacterisation is that Tom has a mere security interest, which, being later in time, is trumped by the bank's. As this is regarded as unfair, UCC–9 and the PPSAs have a special rule which seeks to reverse the consequences of recharacterisation by providing that a "purchase money security interest" (PMSI) has superpriority. However, PMSI superpriority is subject to procedural rules which in practice mean that it may not be attained. In particular, it is a condition of UCC–9 for certain asset classes that "the purchase-money secured party sends an authenticated notification to the holder of the conflicting security interest" before the debtor obtains possession.[17]

Crowther Report

18.9 The Crowther Report was published in 1971.[18] A limited number of its recommendations were implemented by the Consumer Credit Act 1974. Part 5 of the Report called for the adoption of a system based on UCC–9.[19] No draft Bill was attached to the Report.

18.10 Whilst the Crowther Committee considered that the new law based on UCC–9 based should broadly be uniform throughout the UK, it concluded that the substantial differences in the background law as between England and Wales, and Scotland meant that it would be desirable for there to be two separate statutes.[20]

18.11 The Government responded to the Crowther Report with a White Paper, *Reform of the Law of Consumer Credit* (1973).[21] This had very little about Part 5 of the Report, but stated that the Government "were not convinced that the possible benefits of the Committee's recommendations to the credit industry and to some consumers would outweigh the possible social disadvantages to others."[22] The "possible social disadvantages" were not specified. The White Paper added that the Government "will be prepared to reconsider this issue" in the future.

Halliday Report

18.12 Following the Crowther Report, this Commission set up a working party:

> "To consider the legal and technical problems which would arise or be likely to arise in the creation in Scotland of a system of security over moveable property in relation

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[17] UCC § 9–324. But this is not required under either the Australian or New Zealand PPSAs.
[18] The Report of the Committee on Consumer Credit, Cmnd 4596 (1971) chaired by Geoffrey Crowther.
[19] The title of the Crowther Report included the word "consumer". But the Report's recommendation that a UCC–9-type system be adopted was not limited to consumer transactions.
[20] Crowther Report para 5.2.21. But the Report drew heavy criticism from Professor David Walker who argued that its main proposals were "dangers . . . to the fabric of Scots law." See D M Walker, "Crowther's Consumer Credit Chaos Contemplated" 1972 SLT (News) 81 at 85.
[21] Cmnd 5427.
[22] This and the following quotations are from para 8, which seems to be the only paragraph in the White Paper dealing with Part 5 of the Crowther Report.

to all types of loans including consumer loans and to make recommendations in that respect."[23]

18.13 The working party's chair was Professor John (Jack) Halliday, a former Scottish Law Commissioner. Its report, which was submitted in 1983 but only published in 1986, is available on our website. The Report recommended that a UCC–9/PPSA-type approach should be adopted in Scotland. But certain types of property, such as consumer goods, ships, aircraft and intellectual property would be excluded. There would be recharacterisation.[24] There was detailed discussion on ranking and enforcement. In addition, assignations of receivables (even if not by way of security) would have to be registered to be "perfected".[25] The Report had little discussion of floating charges, but like the Crowther Report, it presupposed that they would continue. No legislation followed.

Diamond Report

18.14 In 1985 the then Department of Trade and Industry (a predecessor of the Department for Business, Energy and Industrial Strategy) requested Professor Aubrey Diamond to review the law of security over property other than land. His report appeared in 1989.[26] He too recommended the adoption, in both England and Wales, and Scotland, of a UCC–9/PPSA-type system. Floating charges would disappear as a separate institution.[27]

18.15 For assets in special registers, such as patents, ships etc, Professor Diamond recommended that security rights should continue to be registrable as before, but that additional registration should be required in the new register. A security right registered solely in (say) the patents register would still be valid, but would be invalid in the event of insolvency.[28]

18.16 Professor Diamond agreed with the Crowther Report that whilst the law should be broadly similar on both sides of the Scotland/England border, separate legislation would be desirable.[29]

18.17 The Government rejected the Diamond Report,[30] and so it was not implemented, except for some of the recommendations about Part XII of the Companies Act 1985, which were implemented by Part IV of the Companies Act 1989. However, Part IV was never brought into force.

Murray Report

18.18 In 1994 the Department of Trade and Industry appointed a committee under Professor John Murray QC to review the law of security over moveable property in Scotland.

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[23] Foreword to the Report by Working Party on Security over Moveable Property, March 1986, available at: http://www.scotlawcom.gov.uk/files/8812/8024/7156/Halliday_Report.pdf.
[24] On recharacterisation, see para 18.8 above.
[25] Halliday Report, para 32.
[26] A L Diamond, *A Review of Security Interests in Property* (Department of Trade and Industry, 1989). He benefited from the large number of responses to his preliminary consultation paper. He also took considerable care to learn about Scots law and about views in Scotland.
[27] Diamond Report, para 16.12.
[28] Diamond Report, para 12.3.5.
[29] Diamond Report, paras 8.4.1–8.4.8.
[30] See G McCormack, *Secured Credit under English and American Law* (2004) at 67 for an outline of the reasons given by Government. In brief (i) most people (allegedly) wanted no change, (ii) change would (allegedly) be disruptive and expensive and (iii) there was a possibility that matters would be overtaken by EU legislation.

The committee duly reported.[31] It rejected a UCC–9 approach, apparently on three grounds: (a) the effect on unsecured creditors; (b) its complexity and (c) the fact that it involved notice filing.[32]

18.19 The Murray Report had two main proposals: (i) the introduction of a new fixed security, to be known as a "moveable security" and (ii) the extension of the floating charge.

18.20 The moveable security would be created by registration in a new "Register of Security Interests".[33] This was to be kept by the Registrar of Companies.[34] The new register would have had two parts, one devoted to the new moveable security, and the other to floating charges.[35] The moveable security would be available for corporeal moveable property and would not require possession by the creditor.[36] Consumer goods would be excluded, except in so far as held by a company, such as a manufacturer.[37] So too would ships and aircraft. Only corporeal moveable property owned at the time of the security would be covered.[38] If it were desired to cover after-acquired assets, repeated grants of security would be necessary. The new security would not extend to the proceeds of a sale of collateral by the debtor.[39] The moveable security would also be available for incorporeal moveable property.[40] Intimation would not be required. For receivables, but not for other incorporeal property, the security would be capable of covering after-acquired property.[41]

18.21 In relation to the floating charge, the Murray Report recommended that any debtor should be able to grant this type of security but that in the case of a non-company granter it would be limited to moveables and would not cover consumer goods.[42] As mentioned above, instead of being registered in the Companies Register floating charges would be registered in a new Register of Security Interests. This recommendation and others, including that floating charges would not come into effect before registration, in contrast to the 21-day "invisibility period" that currently exists,[43] are similar to provisions in Part 2 of the the Bankruptcy and Diligence etc. (Scotland) Act 2007. It is discussed in the next section.

18.22 The Murray Report was never implemented.

Bankruptcy and Diligence etc. (Scotland) Act 2007 Part 2

18.23 The last successful attempt at reform of moveable transactions law in Scotland was the introduction of the floating charge in 1961. But, for reasons already mentioned in

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[31] *Security over Moveable Property in Scotland: a Consultation Paper* (Department of Trade and Industry, 1994). For contemporary discussion of the Murray Report, see H Patrick, "Reform of Security over Moveable Property: Some General Comments" 1995 SLT (News) 42 and A J M Steven, "Reform of Security over Moveable Property: Some Further Thoughts" 1995 SLT (News) 120.
[32] Murray Report, paras 2.4–2.5.
[33] Murray Report, para 3.11; Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 22.
[34] Murray Report, para 3.11; Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 22.
[35] Murray Report, para 3.11; Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 22(1).
[36] Murray Report, paras 3.4 to 3.5; Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 9.
[37] Murray Report, para 3.5; Draft Floating Charges and Moveable Securities (Scotland) Bill, definition of "exempt property" at cl 30.
[38] Murray Report, para 3.4; Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 12.
[39] Murray Report, para 3.5; Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 9(3).
[40] Murray Report, para 3.4; Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 9(3).
[41] Murray Report, para 3.4; Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 9(3).
[42] Murray Report, para 3.3. The Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 1 confers the power to create floating charges; clause 30 defines "exempt property" in the case of companies and non-companies.
[43] See para 36.7 below.

Chapter 17, some might question how successful this has been. Floating charges were referred to this Commission for review as part of a wider review of registration of rights in security by companies.[44] In 2004 we published our Report.[45] This recommended a new legislative scheme. There would be a new "Scottish Register of Floating Charges" to be run by Registers of Scotland. Floating charges affecting assets in Scotland would require to be registered there and not in the Companies Register.

18.24 The Report was accepted by the Scottish Government and given effect to by Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007. But, after the legislation was passed, the Committee of Scottish Clearing Bankers wrote to the Scottish Government and argued that it should not be brought into force on the basis that it would result in increased cost to business.[46] The main argument was that whereas a UK company with property in Scotland and England which is to be encumbered by a floating charge has to register only once in the Companies Register under the current law, under Part 2 of the 2007 Act two registrations would be required.[47]

18.25 The Scottish Government then established a technical working group under the auspices of Registers of Scotland to consider the issue. Its report, which was published in 2011,[48] set out three options: (1) implement Part 2 without amendment; (2) implement with amendments; and (3) do not implement. The Scottish Government carried out a consultation on the report in 2012 and has said nothing since. It now appears highly unlikely that Part 2 will ever be brought into force.

Law Commission for England and Wales project

18.26 At the same time as registration of rights in security by companies was referred to us, there was a different and broader reference to the Law Commission for England and Wales, to:

> "(1) examine the law on the registration, perfection and priority of company charges; (2) consider the case for a new scheme of registration and priority of company charges, including charges created by (a) companies having their registered office in England or Wales, wherever the assets charged are located; and (b) oversea companies and companies having their registered office in Scotland, where the charge is subject to English law; (3) consider whether such a scheme should apply both to security in the strict sense and to 'quasi-security' interests such as conditional sales, retention of title clauses, hire-purchase agreements and finance leases, including the extent to and means by which such interests should be made subject to the law governing securities; (4) examine the law relating to the granting of security and 'quasi-security' interests by unincorporated businesses and individuals over property other than land, including the feasibility of extending any new scheme for company charges to such interests, and the extent to and means by which such 'quasi-security' interests should be made subject to the law governing securities; and (5) make recommendations for reform."

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[44] The reference followed on from recommendations in the final report of the Company Law Review Steering Group: *Modern Company Law for a Competitive Economy* (2001).
[45] Scottish Law Commission, Report on Registration of Rights in Security by Companies (Scot Law Com No 197, 2004).
[46] See Register of Floating Charges Technical Working Group: Report to Scottish Government (2011) Appendix 3, available at http://www.scotland.gov.uk/resource/doc/254430/0121799.pdf.
[47] See G Yeowart, "A register of floating charges over Scottish assets: a new "Slavenburg" problem?" (2012) 8 JIBFL 470.
[48] See fn 46.

18.27 Three publications resulted: (i) Registration of Security Interests: Company Charges and Property other than Land (2002),[49] (ii) Company Security Interests: A Consultative Report (2004)[50] and (iii) Company Security Interests (2005).[51]

18.28 Broadly speaking, the first two proposed the adoption, for England and Wales, of a system based on the UCC–9/PPSAs. But whilst there existed strong support for that approach, it also attracted strong opposition.[52] The final report of 2005 therefore contained more limited recommendations. It abandoned two UCC–9/PPSA principles: (i) the recharacterisation of conditional sales, hire-purchase and finance leases as security interests, and (ii) the enactment of a comprehensive code of personal property security law.

18.29 Another difference from the UCC–9/PPSA approach was that the floating charge would continue as a separate institution. But the final report kept another key feature of UCC–9 and the PPSAs, namely that assignments of receivables should be registrable.[53] It also continued to recommend the UCC–9/PPSA registration system of notice filing.[54]

18.30 A new register would be set up, to be called "the Register of Charges and of Sales of Receivables". This would be kept by the Registrar of Companies. This was because the scope of the Law Commission's project was limited to company law. By contrast, a principle of UCC–9 and the PPSAs is that the law of security interests should apply uniformly as between different types of debtor (albeit subject to consumer protection rules) – an approach taken by the great majority of countries round the world which have this type of system. But the Commission's intention was that the system, once established for companies, could later be extended to transactions by non-companies.

18.31 Some of the proposals in the final report were implemented by the Companies Act 2006 (Amendment of Part 25) Regulations 2013,[55] which came into force on 1 April 2013.[56] But many, including the proposals for notice filing and for registration of assignments of receivables, were not. The failure to implement led to the establishment of the Secured Transactions Law Reform Project, which seeks to bring forward recommendations for reform of English law.[57] The City of London Law Society is also working on reform and has produced a draft Secured Transactions Code.[58]

Analysis

General

18.32 The question which naturally follows from the above survey is: why have all these previous attempts to reform secured transactions law been unsuccessful? It is easy to

[49] Consultation Paper No 164.
[50] Consultation Paper No 176.
[51] Law Com Report No 296.
[52] Not least from two influential bodies, the City of London Law Society and the Financial Markets Law Committee. See G McCormack, "Pressured by the Paradigm: the Law Commission and Company Security Interests" in De Lacy (ed), *The Reform of UK Personal Property Security Law: Comparative Perspectives* 83 at 84.
[53] Law Com Report No 296, Part 4.
[54] Law Com Report No 296, Part 3.
[55] SI 2013/600.
[56] See Chapter 36 below.
[57] See https://securedtransactionslawreformproject.org/. See also para 1.32 above.
[58] See City of London Law Society, draft Secured Transactions Code. See para 1.32 above.

answer this. The attempts failed because there was insufficient support for the reform proposed on each occasion, from stakeholders and government. But such an answer does not take us very far, as it leads immediately to the supplementary question: why was there a lack of support? We look at this in turn in relation to (i) a UCC–9/PPSA approach; (ii) the Murray Report; and (iii) Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007.

(i) UCC–9/PPSA approach

18.33 The Crowther, Halliday and Diamond Reports and the Law Commission for England and Wales all supported the UCC–9/PPSA approach, but to no avail. It is possible to identify reasons why. First, this would have been radical law reform and, in the view of many, was too radical. Thus Professor Michael Bridge has written of the Law Commission project: "Drawing upon the wisdom of hindsight, it is possible to say that a more modestly presented series of incremental reforms might have evoked less opposition."[59]

18.34 The second and related reason to this is that the current law does not suffer from the level of inadequacy which afflicted secured transactions law in the USA, Canada and elsewhere prior to the introduction of UCC–9 and the PPSAs.[60] We mentioned above that earlier US law did not recognise the floating charge.[61] Neither does Jersey law.[62] Where PPSAs have been introduced, the new register has typically replaced a multiplicity of previous registers.[63] In the UK, but only in respect of companies and LLPs, there is already a "one stop shop" in the form of the Companies Register.[64]

18.35 The third and again related reason is that the familiarity of current law, notwithstanding its inadequacies, is appreciated by some. Professor Eric Dirix, the architect of Belgium's legislation of 2013 reforming that country's law of security over moveable property, has put it thus: "the modernisation of the system of security rights may not be of the highest priority to the average practitioner, who has only limited information on how other legal systems have evolved. To use the metaphor of the Dutch professor Scholten, when he was contemplating the introduction of a new civil code in the Netherlands, 'It is as if one lives in an old big house. One keeps grumbling about its inconveniences, but after all it is home.'"[65] In the same vein but with a different tone, Professor Hugh Beale, the lead Commissioner on the Law Commission for England and Wales project, has written: "I agree

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[59] M G Bridge, "The Scope and Limits of Security Interests" in H Eidenmüller and E-M Kieninger (eds), *The Future of Secured Credit in Europe* (2008) 180 at 184. See also R Calnan, "What is wrong with the law of security?" in De Lacy (ed), *The Reform of UK Personal Property Security Law* at 187 and N McGrath, "Commentary on the international standards and the reform of English personal property securities law" in N O Akseli (ed), *Availability of Credit and Secured Transactions in a Time of Crisis* (2013).

[60] See eg G McCormack, "Personal Property Security Law Reform in England and Canada" 2002 JBL 113 at 117; H Beale, "The Exportability of North American Chattel Security Regimes: The Fate of the English Law Commission's Proposals" (2006) 43 Canadian Business Law Journal 178 at 186. On the position in New Zealand, see M Gedye, "A Distant Export: The New Zealand Experience with a North American Style Personal Property Security Regime" (2006) 43 Canadian Business Law Journal 208.

[61] See para 18.4 above.

[62] See R Goode, "Reforming the Law of Secured Transactions in Jersey" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 207 at 212. For an overview of Jersey rights in security law, see R F MacLeod, *Property Law in Jersey* (2016) 48–52.

[63] For example, the new Personal Property Securities Register in Australia replaced over 70 separate registers. See http://www.lawsociety.com.au/resources/areasoflaw/PPS/index.htm.

[64] But for criticism see G L Gretton, "Registration of Company Charges" (2002) 6 EdinLR 146. While this article pre-dates the significant changes made to the legislation on 1 April 2013 (see Chapter 36 below), many of the criticisms still hold. Australia had company charges registration legislation before its PPSA, but it too had inadequacies. See A Duggan, "A *PPSA* Primer" (2011) Melbourne University Law Review 865 at 869.

[65] E Dirix, "The New Belgian Act on Security Interests" (2014) 23 International Insolvency Review 171 at 175.

that the current system works – just as steam trains still work".[66] Of course there are also costs in introducing a new system – in particular of setting up the new register and of training lawyers and others – but experiences from elsewhere[67] suggest that this is not a particularly strong argument.

18.36 Fourthly, not all the features of the UCC–9/PPSA approach commend themselves to stakeholders, compared with current English and Scottish law. For example, at the moment there is no need to register and thus incur registration dues in respect of functional securities, such as retention of title and hire-purchase.[68] In contrast, for example, in New Zealand there was a registration regime for motor vehicle hire-purchase agreements prior to the introduction of its PPSA.[69]

18.37 Fifthly, the UCC–9/PPSA approach with its "attachment/perfection" distinction does not fit so easily with Scottish property law as it does with the underlying property law in common law jurisdictions.[70]

(ii) The Murray Report

18.38 The approach taken by the Murray Report was a more limited one. Although there was not implementation as such, the proposals on floating charges influenced Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007. The reasons for the non-implementation are not entirely clear. One may be that the Report was sponsored by the then Department of Trade and Industry in London prior to devolution. Scotland-only commercial law reforms at Westminster are unusual and have to compete with other priorities.

18.39 Five years after the Murray Report and following devolution, the Scottish Justice Minister commissioned research into the "perception that businesses in Scotland are being inhibited in raising capital because, under Scots law, they cannot create a security over moveable property without giving up possession".[71] This led to the publication of the Central Research Unit's Report on Business Finance and Security over Moveable Property (2002). It concluded that there was "little empirical evidence to support the suggestion that business finance is more difficult to obtain in Scotland because SMEs[72] are unable to grant a non-possessory security over moveable assets, or that it is more difficult for unincorporated Scottish SMEs to obtain finance because they cannot grant a floating charge."[73]

18.40 It might be asked: why then is this Commission promoting reform of secured transactions law in the light of that conclusion? First, as we have noted earlier,[74] there was strong support from stakeholders for us to consider this area in the consultation on our Seventh Programme of Law Reform (published in 2006) and Eighth Programme of Law

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[66] Beale, "The Exportability of North American Chattel Security Regimes: The Fate of the English Law Commission's Proposals" at 198.
[67] See Discussion Paper, paras 20.4–20.6.
[68] See eg G McCormack, "Personal Property Security Law Reform in Comparative Perspective – Antipodean Insights?" (2004) 33 Common Law World Review 3 and J Ziegel, "A Canadian academic's reactions to the Law Commission's proposals" in De Lacy (ed), *Reform of UK Personal Property Security Law* 117 at 119.
[69] Motor Vehicles Securities Act 1989. See D Brown, "The New Zealand Personal Property Securities Act 1999" in De Lacy (ed), *Reform of UK Personal Property Security Law* 328 at 332-333.
[70] See para 18.7 above.
[71] Parliamentary Written Answer S1W-1719 (29 September 1999).
[72] Small and medium-sized enterprises.
[73] Business Finance Report at 2.
[74] See para 1.15 above.

Reform (published in 2010) given the deficiencies in the law, which we identified in the previous Chapter of this Report. There was subsequently a high level of support from consultees to the Discussion Paper and also from our advisory group as we worked on this Report. Secondly, the Business Finance Report acknowledged that workarounds are used to circumvent the restrictive nature of the common law, such as hire-purchase, trusts and writing contracts under English law.[75] Implementation of our Report would mean that stakeholders are no longer forced to use such workarounds and instead could use a secured transactions law that is fit for purpose.

(iii) Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007

18.41 This reform failed because, while it would have clearly improved the conceptual coherence of floating charges within Scottish property law, it did not have the support of key stakeholders: the banks. As we saw above, they opposed reform on the basis that it would have potentially increased registration costs.

18.42 We think it true to say that there is a wider point here, namely the desire in the commercial sphere for the law north and south of the Scotland/England border to be similar, if not the same. This can be traced back to the nineteenth century, if not earlier.[76] Thus a reform which pulls Scottish commercial law in a different way from the law of England and Wales is likely to attract opposition from the business community.[77]

18.43 A parallel can be drawn from the experience in Louisiana. Like Scotland, it is a so-called mixed legal system, being influenced strongly by both Roman and English law.[78] Thus it is the only US state with a Roman law heritage. This was essentially the reason why Louisiana was the last state to adopt UCC–9, doing so in 1990. One of the main reasons for the adoption was the desire among financial institutions for there to be a uniformity between Louisiana and the other states, which would facilitate cross-state transactions and reduce transaction costs.[79]

Is now the time for a UCC–9/PPSA approach?

18.44 In the light of the fate of the earlier attempts at reform described above, we concluded in the Discussion Paper that now is not the time for a UCC–9/PPSA approach in Scotland. We said:

> "Some types of reform, such as recharacterisation, would be problematic while English law remains in its present form. For [this and other] reasons, our approach is not to seek perfection[80] in one step. The best can be the enemy of the good, and it seems better to us to develop a reform package that will be major but nevertheless

[75] Business Finance Report at 10–11.
[76] See eg W A Wilson, "Scottish Commercial Law" 1966 JBL 320; Lord Rodger of Earlsferry, "The Codification of Commercial Law in Victorian Britain" (1992) 109 LQR 570; A D M Forte, "A Great Future Behind It? Scottish Commercial Law and the Millennium" (1994) 2 European Review of Private Law 375; Lord Hodge, "Does Scotland need its own Commercial Law?" (2015) 19 EdinLR 299 and J Hardman, "Some Legal Determinants of External Finance in Scotland: A Response to Lord Hodge" (2017) 21 EdinLR 30.
[77] See also Discussion Paper, paras 1.22–1.23.
[78] See eg V V Palmer and E C Reid (ed), *Mixed Jurisdictions Compared: Private Law in Louisiana and Scotland* (2009).
[79] See eg H Gabriel, "Louisiana Chapter Nine (Part One): Creating and Perfecting the Security Interest" (1989) 35 Loyola Law Review 311.
[80] Perfection in the ordinary sense of the term rather than in the UCC–9/PPSA sense.

limited, aware that further reform may be needed, but leaving such further reform until the initial package has been implemented".[81]

18.45 Nevertheless, to test the position we sought the views of consultees on the UCC–9/PPSA approach. Question 4 in the Discussion Paper asked whether they agreed that Scots law should not adopt the attachment/perfection distinction in any of its various forms. All consultees who directly addressed this question agreed. These included the Faculty of Advocates, the Law Society of Scotland, the Judges of the Court of Session and the WS Society. The Judges said: "The paper – it is thought wisely – rejects the complications of making such a distinction". Professor Eric Dirix stated: "I agree with the approach of the Commission. The introduction of the attachment/perfection distinction would add needlessly to the complexity of the system." Scott Wortley said: "I have difficulty in seeing the utility of the attachment/perfection distinction – particularly in a system with a civilian approach to property law."

18.46 Question 80(a) in the Discussion Paper asked consultees whether they agreed that, even if the issue of Article 4 of Directive 2000/35/EC[82] is not an obstacle, Scots law should not, at least at the present time, introduce a system of recharacterisation[83] of quasi-securities. There was unanimous agreement from consultees.[84] Dr Hamish Patrick stated: "Recharacterisation should only be introduced on a UK basis given the consequences for financial institutions and businesses trading throughout the UK." Andrew Kinnes said: "My securitisation and cashflow colleagues were very pleased to hear that the proposals do not include recharacterisation." The WS Society responded: "This is a highly controversial topic and, whatever the arguments for or against, this is exactly what might stand in the way of the other necessary reforms if it is proceeded with."

18.47 In question 80(b) we asked consultees whether, if they agreed with the previous proposal, they thought that Scots law should adopt a "halfway house" in relation to quasi-securities, namely registrability without full recharacterisation. If so, we asked, should it apply to certain cases only (such as trusts) or all cases? Almost all consultees who responded to this question did not favour registration, at least at the present time. This included Dr Ross Anderson, the Faculty of Advocates, the Law Society of Scotland and several law firm consultees. Jim McLean wrote that it would "just be a nuisance and a reason to choose another law." Scott Wortley, however, supported registration of trusts acting as commercial securities. Begbies Traynor, in their response to question 1 of the Discussion Paper[85] favoured a register of trusts.

18.48 Question 80(c) asked whether, if either a full recharacterisation or "halfway house" approach is adopted, there should be categories (for example, sales to consumers) where registration should not be required. It also asked whether there should be grace periods. For most consultees, this question was superseded by their answers to the earlier parts of question 80.

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[81] Discussion Paper, para 1.26.

[82] In the Discussion Paper, para 21.22 we argued that Article 4 of this Directive, which is on combating late payment in commercial transactions, may forbid recharacterisation of retention of title clauses.

[83] On recharacterisation, see para 18.8 above and the Discussion Paper, Chapter 21.

[84] See now also J MacLeod, "Thirty Years After: The Concept of Security Revisited" in A J M Steven, R G Anderson and J MacLeod (eds), *Nothing so Practical as a Good Theory: Festschrift for George L Gretton* (2017) 177 at 190–192.

[85] Question 1 asked if there were other areas of moveable transactions law, not considered in the Discussion Paper, which should be reformed. See para 18.73 below.

18.49 Following these responses, we hold to the position in the Discussion Paper and do not propose a UCC–9/PPSA approach. We are reinforced in this view by the fact that the latest work of the City of London Law Society on reform of secured transactions law in England and Wales, that is to say a draft code, eschews a recharacterisation approach.[86]

Our recommended new scheme

General

18.50 In Chapter 3 of the Discussion Paper we summarised the new scheme on which we sought the views of consultees. Its highlights were that (a) a new register, called the Register of Moveable Transactions ("RMT") should be set up; (b) assignations of claims should be capable of being completed by registration in the RMT as an alternative to intimation to the debtor;[87] and (c) a new security should be introduced, which would be created by registration in the RMT. The new security would be non-possessory for corporeal moveable property and it would also be possible for it to be granted over incorporeal moveable property. For the latter it would thus offer an alternative to transferring the property, for example, financial instruments such as company shares, or intellectual property, such as patents, to the creditor.

18.51 When we suggested this scheme we took account of the lessons to be learned from past unsuccessful reform proposals. While the scheme, if implemented, would amount to major reform, it is less ambitious than the introduction of UCC–9/PPSA legislation. The scheme acknowledges the desire for Scottish commercial law to be broadly consistent with the commercial law of England and Wales. It offers new options for those engaging in moveable transactions. They can choose to use them if they wish. The floating charge and other existing options would continue to be available.

A piecemeal approach

18.52 Our scheme therefore amounts to what can be described as piecemeal law reform. In an important essay, from the standpoint of English law, Professor Louise Gullifer has critically assessed such an approach:

> "There are a number of difficulties with piecemeal reform. First, it only addresses problems that immediately present themselves, rather than considering and tackling problems which have been worked around by market participants or which come from the nature of the system itself. Second, it does not tackle the complexity of the existing system, and may even exacerbate this. Third, considerations of policy underlying the entire system are not considered, only those relating to the specific area being reformed. Fourth, piecemeal reform may be difficult to fit within the existing system; it may give rise to unforeseen inconsistencies, and may, indeed, give rise to more problems than it solves."[88]

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[86] See http://www.citysolicitors.org.uk/attachments/article/121/Secured%20Transactions%20Code%20-%20Discussion%20draft.pdf. Although of course there are others in England and Wales who advocate a UCC-9/PPSA approach. The Secured Transactions Law Reform Project appears sympathetic to it. See https://securedtransactionslawreformproject.org/.

[87] We deal with the assignation aspects of the scheme in volume 1 of this Report.

[88] L Gullifer, "Piecemeal reform: Is it the answer?" in F Dahan (ed), *Research Handbook on Secured Financing in Commercial Transactions* (2016) 421 at 428.

18.53 We consider, however, that at present in Scotland wholesale reform is simply not feasible. This type of reform in other countries has typically involved the adoption of a UCC–9/PPSA-type approach which our consultees rejected. Wholesale reform would also require the replacement of the floating charge, which would go directly against the views of our consultees.[89] It would necessitate too legislation in a number of reserved areas such as the law of business associations, corporate insolvency law and intellectual property law.[90] Even leaving aside the impact of Brexit, the prospect of achieving Scotland-only legislation at Westminster in these areas is in our view very low and the experience of Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007 described above shows that there would be opposition to such an approach.[91]

18.54 The complexity of achieving even piecemeal reform of this area is demonstrated by the fact that it has taken us six years from the publication of our Discussion Paper to present our recommendations in this Report. Wholesale reform would take considerably longer. Even discounting the opposition from consultees, basing new legislation closely on an existing PPSA[92] would not be an easy option to implement as the law of secured transactions needs to fit with underlying property law. As Professor Michael Bridge has noted:

> "A free-standing version of Article 9 cannot be transplanted into another legal system without considerable thought being given to all features of the legal terrain, especially the property law of the receiving jurisdiction, into which it is being transplanted."[93]

The problems caused by the adoption of the floating charge from English law should not be repeated.[94]

Support for the scheme

18.55 The Discussion Paper question 2 asked whether the scheme we proposed would be appropriate. To this question, we received a considerable number of thoughtful responses, containing many helpful points of detail.

18.56 The vast majority of consultees expressed strong support in principle. We quote from the responses of the Asset Based Finance Association (ABFA), CBI Scotland, the Committee of Scottish Clearing Bankers, the Federation of Small Businesses, ICAS/R3[95] and the Scottish Council for Development and Industry in volume 1 of this Report.[96]

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[89] See Chapter 20 below.
[90] See paras 1.39–1.40 above.
[91] See paras 18.41–18.43 above.
[92] As has happened, for example, in Malawi where the NZ PPSA 1999 has been followed. See M Dubovec and C Kambili, "Secured Transactions Law Reform in Malawi: the 2013 Personal Property Security Act" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 183–206.
[93] M Bridge, "Secured Credit Legislation: Functional or Transactional Co-Existence" in S V Bazinas and N O Akseli (eds), *International and Comparative Secured Transactions Law: Essays in honour of Roderick A Macdonald* (2017) 1 at 16.
[94] See para 17.35 above.
[95] Institute of Chartered Accountants of Scotland/Association of Business Recovery Professionals.
[96] See paras 3.20–3.27 above.

18.57 In addition, the then Department for Business Innovation and Skills (DBIS)[97] said: "As a general point we very much welcome the proposal that will allow loans under Scots law to be secured on moveable property."

18.58 In a subsequently published symposium paper, Dr Hamish Patrick commented that:

> "overall the Commission's proposals are to be welcomed, as a pragmatic opportunity to remedy some significant practical defects in the Scottish law of security. They would also appear to have a better prospect of being implemented than previous attempts at reform."[98]

18.59 Similarly, there was support from academic experts, including Professor Eric Dirix, who, as we have mentioned previously, was the leading figure in the recent Belgian reforms, Dr Ross Anderson,[99] David Cabrelli and Scott Wortley. Professor Gerry McCormack said: "In general terms, I think the recommendations in the DP are to be commended as sensible, pragmatic, politically shrewd, in line with international trends and seemingly grounded in commercial realities." Magdalena Raczynska expressed the following view:

> "My overall comment is that it is an excellent and comprehensive paper that seems to target the problems that have arisen in Scotland without being overly ambitious. It has come to my attention during the discussions at the Symposium[100] that there is a concern that the project may not be sufficiently ambitious. Limited ambition is better than over-ambition. There are countless examples of projects, which either never came to fruition despite a desire and good ideas to improve the current law because they were trying to do too much."

18.60 As we worked towards the completion of this Report and finalising our recommendations we kept key stakeholders informed. Colin Borland, Senior Head of External Affairs, Devolved Nations at the Federation of Small Businesses, told us:

> "Today's small businesses need a commercial environment that lets them raise finance against business assets quickly and easily. The current law is rooted in the past and doesn't reflect how business is done. It therefore makes perfect sense to introduce a simple, cost effective method of raising finance against your tangible moveable assets and intellectual property, while allowing you to keep using them."

18.61 When we set out our proposals to the Scotch Whisky Association it consulted its members on these. It subsequently informed us that it believed "in principle, that the proposals would be of benefit to the Scotch Whisky industry".

18.62 ABFA also surveyed its members. Several commented that the ability to take the statutory pledge would decrease the interest rates and fees charged on loans. This effect is supported by empirical studies.[101] ABFA members also commented that the existence of the

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[97] In July 2016 this became the Department for Business, Energy and Industrial Strategy.
[98] H Patrick, "A View from Practice" (2012) 16 EdinLR 272 at 278.
[99] In a subsequently published article Dr Anderson described the Discussion Paper as "excellent". See R G Anderson, "Scottish Share Pledges in the Supreme Court" (2012) 16 EdinLR 99 at 104. Elsewhere he has commented that it "is of the highest quality". See R G Anderson, "Critique" (2012) 16 EdinLR 267 at 271.
[100] See para 1.16 above.
[101] G Castellano, "Reforming Non-Possessory Secured Transactions Laws: A New Strategy" 2015 MLR 611 (; E Benmelech and N K Bergman, "Collateral Pricing" (2009) 91 Journal of Financial Economics 339; J R Booth and L C Booth, "Loan Collateral Decisions and Corporate Borrowing Costs" (2006) Journal of Money, Credit and Banking 67 and World Bank, "Getting Credit: The Importance of Registries" (2014) in *Doing Business 2015: Going Beyond Efficiency*.

statutory pledge would encourage them to provide more finance than they currently do to businesses in Scotland.

18.63 The Finance and Leasing Association also sought the views of its members. Again there was significant support for our proposals. One member commented:

> "I am sure all funders will agree – anything which makes the security position in Scotland more accessible and transparent will be welcomed. The [Commission's proposals] certainly sound like they would achieve this."

18.64 In July 2017 we consulted on an advanced version of our draft Bill and again consultees were broadly supportive of the security provisions within it.

Doubts, concerns, opposition

18.65 The Judges of the Court of Session and the Faculty of Advocates expressed doubts about whether reform of the law was needed. The Judges referred directly to the opposition to the earlier proposals[102] of the Law Commission for England and Wales:

> "Given the importance of some degree of coherence between the positions north and south of the border, this state of affairs in England and Wales raises a question as to the prudence of proceeding with major law reform in this area in Scotland."

In our view, this overlooks the point that there is a more pressing need for reform north of the border, for the reasons set out in Chapter 17. Further, the proposed scheme eschews the UCC–9/PPSA approach because of the need for there to be consistency with the law of England and Wales.

18.66 While the Faculty praised the Discussion Paper as "a significant and positive contribution to the development of the law in an important field", it noted the apparent lack of empirical evidence in relation to businesses facing difficulties in obtaining loan finance. It then said: "therefore there is reason to question whether the reforms proposed to the law of security are commercially necessary". For the reasons set out in Chapter 17 and in the BRIA, and given the strong support for reform from other consultees, we disagree. The Faculty also raised the difficulty of trying to reconcile the need to make the proposed new security right a "strong" security which banks and financial institutions would favour with the need to protect good faith third parties who in certain transactional contexts cannot be expected to search the new register. But this challenge is not unique to Scotland. Modern legislation in other jurisdictions endeavours to strike a balance in this respect and this is our approach too.[103]

18.67 Others had concerns on issues of detail. Three deserve comment here as they were shared by a number of consultees. The first was the proposal that the new security should have both a fixed and floating nature. This came in for criticism as not being sufficiently explained. Several consultees felt also that the case for a floating version, referred to in the Discussion Paper as a "floating lien", would create an unnecessary and untidy overlap with the floating charge. We accept these criticisms for the reasons given in more detail in Chapter 20. We now recommend that the new security right is fixed only.

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[102] See paras 18.26–18.31 above.
[103] See Chapter 24 below.

18.68 The second concern, expressed by the Law Society of Scotland, a number of law firm consultees and Jim McLean, was whether it was sensible for the scheme to apply to consumers. When we explored this concern with some of these consultees, they stated that they considered that there was a more pressing need for reform in a business context and they did not wish to see that reform being delayed by consumer specialities. We have given this issue considerable thought and discussed it with other stakeholders including the FLA and the Consumer Credit Trade Association. As discussed further in Chapter 19, we hold to the view in the Discussion Paper, that the scheme should apply to consumers, but with appropriate protections. This is in line with comparator legislation elsewhere.

18.69 Thirdly, there was concern about the inter-relationship of the scheme with insolvency law. The Faculty of Advocates, Scott Wortley and Donald McGruther CA criticised the fact that insolvency law was not considered in the Discussion Paper. Tom Hughes CA stated: "I have reached the conclusion that Insolvency Law as a whole needs overhauled, particularly in the corporate sector." But to have added insolvency law and then, necessarily, the related area of diligence to the scope of the project would have made it considerably larger and resulted in publication of this Report taking many more years. This Report is already one of the largest that this Commission has ever published. Moreover, there is the significant complication that personal insolvency law is devolved to the Scottish Parliament but corporate insolvency law is reserved to the UK Parliament. The principal statute is the Insolvency Act 1986. Work to reform corporate insolvency law would therefore clearly need to proceed on a UK-wide basis. Our approach follows that of the Law Commission for England and Wales, which in its project on company security rights said that the reforms that were being proposed would not make significant changes to insolvency law.[104] In any event some of the Faculty's more specific concerns in relation to insolvency law concerned the "floating lien", which we are now not pursuing.[105]

18.70 There was more particular anxiety about the effect of our scheme on unsecured creditors and on meeting the expenses of an insolvency, a view expressed trenchantly when we convened a meeting with insolvency specialists in September 2015 to discuss the impact of our likely recommendations.[106] These points were also made by ICAS and R3 in their responses to our draft Bill consultation in July 2017. It was argued that if there were additional ways in which to create security then there would be less left for creditors who do not take security. While there is some force in this, for a number of reasons we do not think it is a compelling justification simply to leave the law unreformed in its current unsatisfactory state.

18.71 First, the new scheme would enable creditors who are unsecured at present, due to the restrictive nature of the current law, to take security. Secondly, the scheme in many situations is aimed at allowing security to be taken in a more efficient way than existing forms of security. Thus instead of having to transfer shares in a company to a bank, the new security right (the statutory pledge) could be used. Instead of assigning a patent, the

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[104] See eg Law Commission, Registration of Security Interests: Company Charges and Property other than Land (Law Com CP No 164, 2002) para 3.411.

[105] See Chapter 20 below.

[106] We are grateful to the representatives of ICAS/R3 and others who attended that meeting. We have particularly appreciated the help of Donna McKenzie Skene of the University of Aberdeen and Roy Roxburgh, formerly of Maclay, Murray & Spens in relation to the interface of the project with insolvency law.

statutory pledge could be granted over it.[107] Thirdly, we expect the statutory pledge to be used mainly by companies and LLPs. The insolvency of these entities is regulated by the Insolvency Act 1986, which as mentioned above, applies both in Scotland, and in England and Wales. In functional terms, the new security right is the equivalent of the English fixed charge. Thus the effect of the scheme is to put secured creditors of Scottish companies and LLPs on the same footing as the secured creditors of English and Welsh companies and LLPs against a common insolvency-law background. Fourthly, we have modified our proposals in the Discussion Paper by not proceeding with the floating lien. The reasons for this are discussed in Chapter 20. This would reduce the effect on unsecured creditors, particularly of non-corporate bodies. Fifthly, for reasons discussed further in Chapter 22, we recommend that the scope of the statutory pledge at least initially is limited to two classes of incorporeal moveable property: financial instruments and intellectual property. This would lessen its effect on other interests in an insolvency. Sixthly, retention of title would remain possible and sellers of goods would be able to protect themselves through that device, although suppliers of services would not have this option available to them. Seventhly, because of the restrictions which we recommend below in relation to the grant of a statutory pledge by private individuals we think that its introduction would have little impact on non-business insolvencies.[108]

18.72 There was very limited opposition in principle to the scheme. The principal opponent was Chris Dun.[109] In his consultation response he stated his view that the current law was "incompatible with modern commercial practice." But he was "wary in particular of a solution which involves yet another register. This seems to create a cumbersome system." He had several concerns. But we believe that we can offer some reassurance regarding these. First, he was worried that the scheme would supersede the current law. It would not. The scheme would supplement the current law and provide parties with further options. Secondly, he was concerned about recharacterisation. We do not recommend recharacterisation. Thirdly, he did not want to see the loss of the floating charge. We recommend the retention of the floating charge. Mr Dun favoured a solution which "would allow for the grant of a security over moveable property without notice, but with specified protections to third parties without notice." Here we differ from him, as the trend internationally is very much for a register-based system because it improves transparency. Systems such as those in Germany and the Netherlands, where registration is not required, are coming under increasing critical scrutiny in this regard.[110]

Issues not covered in the Discussion Paper

18.73 We also asked consultees if there were any issues in the field of moveable transactions law that stand in need of reform that were not covered by the Discussion Paper.[111] Only a few additional issues were mentioned. One was insolvency law, which we

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[107] Although we accept that the new security could be taken by several creditors over the same asset, whereas a transfer can only be to one.
[108] See paras 19.36–19.51 below.
[109] Mr Dun kindly agreed to join our advisory group in 2014.
[110] See eg A Morell and F Helsen, "The Interrelation of Transparency and Availability of Collateral: German and Belgian Laws of Non-possessory Security Interests" (2014) 22 European Review of Private Law 393; Hamwijk, *Publicity in Secured Transactions Law* ch 4 and M Brinkmann, "The Peculiar Approach of German Law in the Field of Secured Transactions and Why it Has Worked (So Far)" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 339–354.
[111] Discussion Paper, para 1.42.

cover above. As mentioned earlier,[112] Begbies Traynor argued for a register of trusts, but when we canvassed such a possibility in our trusts project it drew strong opposition.[113] Professor Stewart Brymer suggested that there might be a register of ownership of moveable property such as vehicles. This is outwith our scope.

Conclusion

18.74 As we have seen, most of our consultees supported the scheme set out in the Discussion Paper, although there were comments on detail, which we have taken account of in preparing this Report. In particular, we consider now that the new security should be fixed only and there should not be a floating lien. A modestly revised version of the scheme is set out above in Chapter 16. We recommend that:

71. The law on security over moveable property should be reformed on the lines set out in Chapter 16.

[112] See para 18.47 above.
[113] Scottish Law Commission, Report on Trust Law (Scot Law Com No 239, 2014) paras 3.9 and 3.11.

Chapter 19 Security over moveable property: general

Introduction

19.1 In Chapter 18 we set out the support from consultees in relation to the reform of security over moveable property in Scotland along the lines of the scheme described in the Discussion Paper. Central to that scheme was the proposal to introduce a new form of security right which would require registration. The security right would be a "true" security. Ownership would remain with the party granting the security right and the secured creditor would acquire a subordinate right in the property.

19.2 As regards corporeal moveable property the new security right would be *non-possessory*. It would complement the existing security right of pledge, which is *possessory.* For the reasons explained fully in the following chapter we recommend that the new security right should be a fixed security only. Pledge too is a type of fixed security. The essential difference between the two types is that one is created by delivery (placing the secured creditor in possession of the property being encumbered) and the other would be created by registration. As we shall explain, this has influenced our recommendation below that the new security right should be called a "statutory pledge". This approach has the advantage of enabling some of the core rules of possessory pledge to be placed on a modern statutory footing and facilitating a broadly common battery of enforcement remedies for both types of security right.

A new type of pledge

19.3 If a new security right over moveable property is to be introduced it requires a name. In the Discussion Paper we expressed the view that a snappy name would be desirable.[1] There we used "new moveable security" as a working title, but we were clear that this was all it could be, as this term would not be suitable for legislation. The Murray Report[2] used the term "moveable security" for its proposed security, which would have been competent in relation to corporeal moveable property (without possession) and incorporeal moveable property (without intimation). While that term provides a match with "heritable security" it suffers from the flaw that "moveable security" (like "heritable security") is a more generic term and this is capable of including pledge, aircraft mortgages, ship mortgages etc.[3] In the Discussion Paper we suggested "registered moveable security", which we noted, was not very snappy. Again, however, there are other registered moveable securities, such as the floating charge. Another possible name - "moveable hypothec" - is imperfect because

[1] Discussion Paper, para 16.82.
[2] See paras 18.18–18.22 above.
[3] See A J M Steven, "Reform of Security over Moveable Property: Some Further Thoughts" 1995 SLT (News) 120.

"hypothec" means non-possessory security[4] and, in general terms, only corporeals and not incorporeals can be possessed.[5] Further, it is not a familiar term to non-lawyers.

19.4 In response to our question as to what the new security right should be called, we had a variety of responses from consultees. David Cabrelli favoured "moveable security". The Aberdeen Law School and Chris Dun both suggested "moveable property security". John MacLeod thought "registered moveable security" was appropriate. Dr Ross Anderson suggested a formulation using the word "hypothec".[6] Dr Hamish Patrick had no strong views, but mooted "moveable security interest". Several law firm consultees as well the Law Society of Scotland did not have strong opinions. Magdalena Raczynska proposed "charge",[7] but this is a technical term in English law and might lead to possible confusion with the floating charge. The Keeper of the Registers of Scotland considered it important that the new form of security should be given a name that is simple, descriptive and not easily confused with other forms of security or diligence.

19.5 There was thus no consensus among consultees as to what would be an appropriate name. We have given the matter careful consideration and ultimately we have decided on the name "statutory pledge".[8] Our reasons are as follows. First, "pledge" is a familiar word in the context of rights in security and the word has an additional sense, namely "promise".[9] The party granting the security is promising that the asset being encumbered will be available to the secured creditor if there is default. Moreover, other jurisdictions use the term "pledge" in the context of their law of rights in security over moveables. Examples include French law in relation to the equivalent term "gage",[10] German law in its use of "Pfand"[11] and Dutch law in relation to "pand".[12] Sometimes, as in French law, the term is restricted to corporeal moveables.[13] Sometimes it is not.[14] We note also that the English translation of recent important and broad-ranging legislation reforming security over moveable property in Belgium is the "Belgian Pledge Act of 11 July 2013".[15]

19.6 Secondly, the name is relatively snappy. Thirdly, for the reasons which we give in the next chapter, the new security right, like pledge, is to be a fixed security only. Fourthly, this approach effectively creates a second type of pledge in Scottish law. The common law possessory pledge gains a brother or sister, the statutory pledge. But, being siblings, it is possible to apply common terminology and rules to them. In particular, it allows their enforcement rules to be put onto the same footing, a matter which we discuss further in Chapters 27 and 28 below. As we say there, it is difficult to see why there should be

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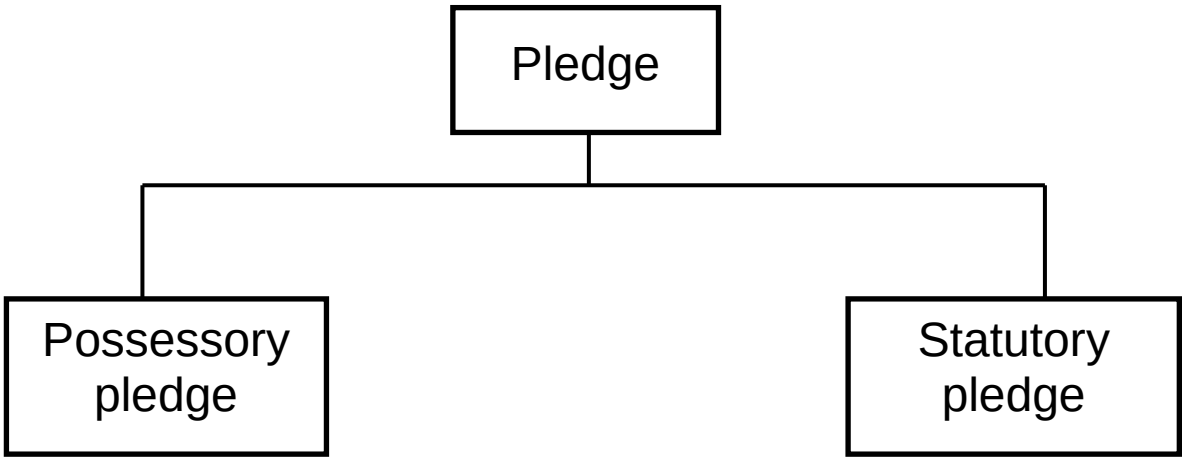
[4] Stair 1.13.14; Gloag and Irvine, *Rights in Security* 406.
[5] The subject is not without controversy. See eg T Rüfner, "Possession of Incorporeals" in E Descheemaeker (ed), *The Consequences of Possession* (2014) 171.
[6] See also R G Anderson, "A Critique" (2012) 16 EdinLR 267 at 271.
[7] This name was also suggested to us informally by Richard Calnan.
[8] We also considered the term "registered pledge", a term which was independently suggested to us by Dr Craig Anderson when we consulted on our draft Bill in July 2017. The difficulty with this term is that in some instances because of the Financial Collateral Arrangements Regulations the new security can be created without registration. See Chapter 37 below.
[9] See Steven, *Pledge and Lien* para 2-04.
[10] French Civil Code art 2337.
[11] German Civil Code §§ 1204–1296.
[12] Dutch Civil Code arts 3:236–3:259.
[13] For incorporeal moveables the term is "nantissement". See French Civil Code art 2355.
[14] The term "pand" is used broadly in Dutch law for security over moveable property, including over financial instruments and intellectual property.
[15] See E Dirix, "The New Belgian Act on Security Interests in Movable Property" (2014) 23 International Insolvency Review 171.

different enforcement remedies depending on whether a security right has been perfected by possession or registration. This indeed is the position under UCC–9 and PPSAs.

19.7 The result of this approach is shown by the diagram below.



19.8 We recommend that:

72. (a) There should be a new right in security over moveable property.

(b) It should be a new type of pledge called a "statutory pledge".

(Draft Bill, s 43(1), (2)(b) & (4))

The parties

General

19.9 In the draft Bill we use the term "provider" for a person who grants a pledge, be that a possessory pledge or statutory pledge. The person in whose favour the pledge is granted is referred to as the "secured creditor".[16]

19.10 It might be thought that an obvious term for the granter of the security right is the "debtor". This is the term used in UCC–9[17] and some of the PPSAs.[18] Nevertheless, it is possible for the person owing the debt and the granter of the pledge to be different persons. This is known as third-party security.[19] For example, Simon could grant a statutory pledge over his car to a bank in respect of a loan by the bank to his wife Tamsin. In doing this Simon does not become personally liable for repayment, but if the debt is not repaid the car

[16] We have been influenced here by the DCFR IX.–1:201(12) and (13).
[17] UCC § 9–102 (a) (28).
[18] Eg NZ PPSA 1999 s 16(1).
[19] See Gretton and Steven, *Property, Trusts and Succession* para 21.19. See also Drobnig and Böger, *Proprietary Security in Movable Assets* 271–272 and 273–274. See too the Belgian Pledge Act of 11 July 2013 art 10 (which provides for art 5 of the new Book III title XVII of the Civil Code).

will have to be sold. In other words, the right of the bank against Tamsin is secured over Simon's car. Thus Simon is the provider of the security and Tamsin is the debtor.

19.11 We favour the terms "provider" and "secured creditor" over "pledger" and "pledgee", which are used in the context of the existing law of pledge, because they are more generic terms used in modern legislation on security rights elsewhere. They are also, we consider, more accessible to lay persons.

19.12 We recommend:

73. (a) The person to whom a pledge is granted should be referred to as the "secured creditor".

(b) The person who grants the pledge should be referred to as the "provider".

(Draft Bill, s 43(5))

Successors

19.13 The parties to the pledge may not stay the same. Thus the pledge might be assigned to a new secured creditor. The provider may die and the provider's property then would vest in the executor. It is important therefore that the terms "provider" and "secured creditor" include successors. Equivalent provision is made in the legislation on standard securities.[20]

19.14 In the case of the provider, the definition should include successor owners of the encumbered property, against whom the pledge can equally be enforced. On the other hand successor owners who take the property free of the pledge because of the good faith acquisition provisions which we recommend elsewhere[21] should not be included.

19.15 We recommend:

74. (a) The term "provider" should include any successor in title or representative of a provider (unless the successor or representative is a person who acquired the encumbered property unencumbered by the statutory pledge in question).

(b) The term "secured creditor" should include any successor in title or representative of a secured creditor.

(Draft Bill, s 116(1))

[20] Conveyancing and Feudal Reform (Scotland) Act 1970 s 30(1) (definitions of "creditor" and "debtor"). And see also the Belgian Pledge Act of 11 July 2013 art 29 (which provides for art 24 of the new Book III title XVII of the Civil Code).

[21] See Chapter 24 below.

What is secured?

Terminology

19.16 It is commonly understood that security rights secure the payment of debts.[22] Thus Neil may buy a house with a loan from a bank. In return the bank obtains a standard security (known to the layperson as a "mortgage") from Neil. This means in principle that the house can be sold to satisfy the debt if Neil fails to keep up his loan repayments. Thus, the Conveyancing and Feudal Reform (Scotland) Act 1970, provides that: "A grant of any right over land or a real right in land for the purpose of securing any debt by way of a heritable security shall only be capable of being effected at law if it is embodied in a standard security."[23]

Monetary and non-monetary obligations

19.17 Normally, a security right will secure the payment of a monetary debt.[24] But sometimes security rights are granted in respect of non-monetary obligations.[25] Thus the 1970 Act defines "debt" as including an obligation *ad factum praestandum*, in other words an obligation to do something.[26] While a pledge should be capable of securing performance of a non-monetary obligation, ultimately all that can be obtained from enforcement of a security against an asset is money. Thus it would seem that what is actually secured is the right to payment of damages if there is default.[27] Unless there is a liquidated damages clause in the security agreement, enforcement against the asset is problematic.

Restricted or unrestricted?

19.18 Security rights can either be restricted or unrestricted.[28] A restricted security right secures a fixed amount. Thus John may pawn his watch to a pawnbroker for £100. The watch only secures the repayment of the £100 and no other debts. In contrast, an unrestricted security right secures all sums owed by the debtor to the secured creditor. This is the normal position for standard securities. Take the following example. April buys a house for £200,000 with the help of a £150,000 loan from a bank. In return the bank will take a standard security, which it will register in the Land Register. The standard security will state that it secures "all sums due and to become due". This means that if April borrows further money from the bank, say to add a conservatory, that sum would also be secured. The unrestricted security avoids the expense and inconvenience of having to grant a fresh security.

19.19 In the Discussion Paper we proposed that the rule for the new type of security right should be the same as for standard securities. In other words, the statutory pledge would be

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[22] Strictly what is the secured is the right to performance of the debt. See DCFR IX.–2:401. But the terms "secured debt" and "secured obligation" are in general usage. See eg UNCITRAL Model Law on Secured Transactions article 7 and City of London Law Society draft Secured Transactions Code section 18 (pp 62–65).
[23] Conveyancing and Feudal Reform (Scotland) Act 1970 s 9(3).
[24] On the different meanings of the term "debt", see M Hogg, *Obligations: Law and Language* (2017) 54–60.
[25] For common law examples, see *Moore v Gledden* (1869) 7 M 1016 and *Edmonstone v Seton* (1886) 16 R 1.
[26] Conveyancing and Feudal Reform (Scotland) Act 1970 s 9(8)(c). See also the Companies Act 1985 s 462(1) which provides that floating charges can secure "any debt or other obligation (including a cautionary obligation)."
[27] See G L Gretton, "The Concept of Security" in D J Cusine (ed), *A Scots Conveyancing Miscellany: Essays in Honour of Professor J M Halliday* (1987) 126 at 128–129. See also D J Cusine and R Rennie, *Standard Securities* (2nd edn, 2002) para 3.05.
[28] See eg Gretton and Steven, *Property, Trusts and Succession* para 21.16.

unrestricted. It could be granted not only for existing obligations but for future obligations too. But of course the parties would be free to agree that the security right should be for a restricted amount. The approach under UCC–9,[29] the PPSAs,[30] the DCFR Book IX[31] and the UNCITRAL Model Law on Secured Transactions[32] is the same.

19.20 We asked consultees whether they agreed that the new security right should be capable of securing the performance of future obligations. Almost all the consultees who responded to this question agreed. One law firm[33] said: "this is an obvious requirement and is what financiers expect. Legislative certainty on the point would be advantageous to Scotland as a commercial destination." The WS Society stated: "this appears to be common sense and to tally with what is done in practice with most commercial security in the banking and finance world at present . . . why have different rules for securities over different types of asset?" Brodies said: "We are clear that this should be possible and is entirely consistent with market participant expectations." Aberdeen Law School agreed in principle, subject to there being a "quick, cheap and effective way" for individuals who have granted the security to check the new register in which the security appears. We discuss searching the register in Chapter 34 below.

19.21 Scott Wortley was the sole consultee against the new security right being unrestricted. He was concerned about the effect on unsecured creditors of introducing a new security right. We discuss this concern elsewhere.[34] We think, however, that it would be anomalous and commercially unattractive for the statutory pledge to be restricted to a fixed sum when the floating charge and the standard security are not. It would also make Scottish law inconsistent with the position under comparator legislation, the DCFR and the UNCITRAL Model Law, and could potentially make Scotland a less attractive place for lending by foreign-based financial institutions.

19.22 In relation to possessory pledge, the current law is unclear as to whether the debt can be unrestricted, although there is authority to suggest that it can.[35] We see no reason why a possessory pledge should be different from a statutory pledge. It should be capable of being unrestricted.

Other aspects of the secured obligation

19.23 Earlier we discussed how the secured obligation need not necessarily be an obligation against the provider. We gave the example of the bank's right to repayment by Tamsin of its loan secured against a car owned by Simon.[36] We think that the permissibility of this type of arrangement should be stated expressly.

19.24 Where the pledge has been granted in favour of a security trustee, the secured obligation(s) would be owed to the creditors for whom the trustee holds the pledge. But for the purposes of the draft Bill, the trustee would be the "secured creditor", as it is the grantee

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[29] UCC § 9–204(c).
[30] Eg Saskatchewan PPSA 1993 s 14(1); NZ PPSA 1999 s 71; and Australian PPSA 2009 s 18(4).
[31] DCFR IX.–2:104(5).
[32] UNCITRAL Model Law on Secured Transactions art 7.
[33] Dundas & Wilson.
[34] See paras 18.69–18.71 above.
[35] Steven, *Pledge and Lien* paras 4-03–4-17.
[36] See para 19.10 above.

of the pledge. It should be therefore made clear that the secured obligation may be owed to a person other than the "secured creditor".

19.25 The secured obligation should also include ancillary obligations of the provider, for example to pay interest, to pay damages (for non-performance) and to pay the reasonable expense of extra-judicial recovery of interest and damages.[37]

19.26 We therefore recommend that:

> **75. The secured obligation:**
>
> **(a) may be any obligation owed, or which will or may become owed, to the secured creditor,**
>
> **(b) should not require to be an obligation owed**
>
> **(i) by the provider, or**
>
> **(ii) to the secured creditor, and**
>
> **(c) should include ancillary obligations owed to the secured creditor (as for example to pay interest, damages or the reasonable expenses of extra-judicial recovery of interest or damages).**
>
> (Draft Bill, s 44(2))

Non-accessory security

19.27 A security right is an "accessory" right.[38] It is dependent on the secured obligation. Thus the secured obligation, normally a monetary debt, is the principal and the security right is the accessory. As we have seen, it is not necessary for the debtor and the provider to be the same person.[39]

19.28 It is also not necessary for there to be a present secured obligation, merely that it is possible for there to be a secured obligation. For example, a company can grant a floating charge to a bank in respect of an overdraft facility. But the facility might never be used. There might never actually be a secured debt, but as long as the coming into being of a secured debt is possible a security may validly be granted.[40] In contrast a stricter approach is taken with some security rights, particularly historically, in that a present debt is required.[41]

19.29 Some legal systems, notably Germany and Switzerland, have developed non-accessory security in relation to land, although the concept is not without its problems.[42] In

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[37] See DCFR IX.–2:401. See also the Belgian Pledge Act of 11 July 2013 art 17 (which provides for art 12 of the new Book III title XVII of the Civil Code).
[38] Discussion Paper, para 5.28.
[39] See para 19.10 above.
[40] See A J M Steven, "Accessoriness and Security over Land" (2009) 13 EdinLR 387 at 399–400.
[41] In her consultation response Magdalena Raczynska noted this was the traditional position in Polish law.
[42] Not least where the security is assigned, but the security contract is not so that the security can be enforced although there is no actual debt. In Germany this led to the introduction of the *Risikobegrenzungsgesetz* in 2008 in order to let the debtor plead any defence arising out of the security agreement against a subsequent holder of the security. See generally L P W van Vliet, "Mortgages on immovables in Dutch law in comparison to the

the Discussion Paper,[43] we expressed our understanding that there can be situations where a company wants to raise money on the security of certain assets, without being contractually liable for the loan. Thus if the company defaults, the creditor can enforce against the property, but if this does not satisfy the debt, the creditor cannot sue the company for the deficit. We considered that this can be achieved by contractual agreement that the creditor will not enforce its right to recover the debt by personal action. But, nevertheless, we asked consultees whether non-accessory security over moveable property should be competent.

19.30 There was only limited support for this. The Faculty of Advocates answered "yes" but gave no reasons. Chris Dun was in favour, subject to protection for third parties without notice. Dr Ross Anderson considered that non-accessory security should in principle be competent, but thought that the demand was greater for security over land rather than over moveables. Magdalena Raczynska favoured a diluted version of non-accessory security to ensure debtor protection, noting recent problems in German law. David Cabrelli, Dr Hamish Patrick, the WS Society and several law firm consultees were unpersuaded of the need for legislative intervention here. Professor Eric Dirix noted that non-accessory security rights are unknown in the civil law tradition. Scott Wortley argued that any reform should be considered in the context of the law of rights in security as a whole and not for moveables only. We conclude that the case for the statutory pledge (or indeed possessory pledge) to be capable of being non-accessory has not been made out and recommend:

76. There should not be a non-accessory form of pledge.

Who can grant?

19.31 In general any person can grant a security right, provided of course that the person has a relevant asset.[44] Thus the owner of a house can grant a standard security over that property. The owner of a watch may pledge it. The owner of a ship can grant a ship mortgage over that vessel. There is one notable exception to this general principle. Only companies and a limited number of other corporations[45] can grant a floating charge.

19.32 In the Discussion Paper we asked whether any person, juristic or natural, should be able to grant the new security. This question was asked in the context of the proposal that the new security should have a floating version, a proposal from which, as will be explained in the next chapter,[46] we have now departed. Nevertheless, the question remains valid at the more general level.

19.33 An overwhelming majority of the consultees who responded to this question agreed that any person should be able to grant the new security right. Several, including ABFA, Dr Ross Anderson and the WS Society noted that this would be particularly helpful for partnerships, which of course are unable to grant floating charges. A few consultees, including the Faculty of Advocates, had doubts about whether consumers should be able to grant the security. Our view, in line with the position under comparator legislation in

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German mortgage and land charge" in M Hinteregger and T Borić (eds), *Sicherungsrechte an Immobilien in Europa* (2009) 285 at 293–297.

[43] Discussion Paper, para 5.29.

[44] Or in the future may have a relevant asset.

[45] Including limited liability partnerships. See para 17.30 above.

[46] See Chapter 20 below.

numerous other jurisdictions, is that they should.[47] They should, however, be protected by certain consumer-specific provisions. We discuss this subject below.[48] The availability of the statutory pledge to consumers was also something which was supported by the Finance and Leasing Association and the Consumer Credit Trade Association in post-consultation discussions with them.

19.34 For possessory pledges it has always been the case that any person can grant this type of security right.

19.35 We therefore recommend:

77. Any person, juristic or natural, should be able to grant a pledge.

Protection for consumer providers of statutory pledges

General

19.36 The Consumer Credit Act 1974, as well as containing generic provisions on security rights granted by consumers,[49] sets out certain protections in relation to pledges by "individuals"[50] to pawnbrokers.[51] These provisions would continue to apply to possessory pledges by such individuals under our new scheme.[52] These do not, however, limit the classes of asset that can be pledged.[53]

19.37 There are, however, two major differences between possessory pledge and the new statutory pledge, which make it necessary to consider restricting the availability of the latter. The first is that because the statutory pledge would be a non-possessory security, providers (usually debtors) would not need to relinquish direct possession of their assets. Having to hand the item over concentrates the mind as to whether one can do without it. The second difference is that the statutory pledge, as we shall see in the next chapter, would be capable of being granted over future assets. In principle, someone could grant a statutory pledge over not just their current vehicle, but all future vehicles that the person may come to own. The consequences could be significant.

19.38 In the Discussion Paper we noted that UCC–9 and the PPSAs broadly speaking do not allow security over after-acquired consumer goods.[54] The DCFR in general does not allow security to be granted by consumers over after-acquired property.[55] We noted that there is a difference between these approaches, the one restriction relating to the type of property and the other to the type of granter. We said that we inclined to the DCFR formulation and we asked consultees whether they agreed that the new security right should

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[47] See also para 18.68 above.
[48] See paras 19.36–19.55 below.
[49] See in particular Consumer Credit Act 1974 ss 105–113.
[50] This term is defined more widely than might be expected. See para 19.52 below.
[51] Consumer Credit Act 1974 ss 114-122. As we note at paras 1.39–1.42 above the subject matter of the 1974 Act is reserved to the UK Parliament. Our draft Bill is intended to within the competence of the Scottish Parliament and therefore has no provisions amending the 1974 Act. The provisions which it has on consumer protection are specific to the statutory pledge and would also be subject to the more general provisions on security rights in the 1974 Act.
[52] See para 27.17 below.
[53] But see the more general provision in the 1974 Act s 123(3) on negotiable instruments being taken in security from consumers.
[54] Discussion Paper, para 16.75.
[55] DCFR IX.–2:107(1)(b).

not be capable of being granted by a consumer in relation to future property. Consultees generally agreed and we so recommend.

19.39 In the Discussion Paper we went on to ask whether there should be other restrictions in relation to consumer debtors.[56] For example, should goods exempt from diligence be excluded? We noted, however, that goods that are exempt from diligence can still be subject to hire-purchase etc. It may be thus argued that to exclude such property from the scope of the new security right would be merely to encourage the use of hire-purchase, which in itself is an artificial system. We also made the suggestion that the security right should be valid only to secure purchase finance.

19.40 There was in general strong support from consultees for further restrictions, but differences as to the detail. Brodies, David Cabrelli, John MacLeod, Dr Hamish Patrick and the Law Society of Scotland supported the exclusion of goods exempt from diligence. Chris Dun stated that ordinary household items should be excluded. We agree that there should be protection in respect of such items. As a matter of social policy, individuals clearly should not be able to grant a statutory pledge over their cooker, clothes, bedding or children's toys, even if in practice secured creditors may be unlikely to be interested in such items.[57] The question, however, is whether drawing on the list of goods exempt from diligence is the best way of achieving that policy.

19.41 It is the Debt Arrangement and Attachment (Scotland) Act 2002 which specifies which goods are exempt. There is not a single list. The exclusions are set out across a number of provisions and are not particularly accessible.[58] Some of the provisions are nuanced, for example a vehicle will be excluded if it is not worth more than £1,000 and its use is reasonably required by the debtor.[59] It is sheriff officers in the main who must master the list. For the statutory pledge any would-be creditor would in principle have to know the list. Perhaps this concern is not strong, as the banks and other professional credit providers would usually be the creditor and they would be able to familiarise themselves with the list. But there remains the "nuanced" issue. A sheriff officer,[60] with whom we discussed the list, stressed that many of the items on it are subject to qualifications such as being "reasonably required" by the debtor.

19.42 We think that there may be a simpler way of achieving the desired policy. This is that there should be a prohibition against individuals granting a statutory pledge over items worth less than a figure to be set by statutory instrument. The amount which we have currently in mind is £1,000, a figure which appears in various places in the list in the 2002 Act. This would exclude essential personal and household items such as ordinary clothes, bedding, furniture, white goods and toys. Most televisions would be excluded too. It is likely that the item that would most commonly be the subject of a statutory pledge granted by a consumer would be a motor vehicle. We were advised by Bruce Wood that valuable musical

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[56] Discussion Paper, para 16.78.

[57] A similar argument for protection was made by the City of London Law Society in its response to the Law Commission for England and Wales' consultation on bills of sale but this was rejected by the Commission on the ground that "there was little indication that lending secured on essential household goods is, or would become, commonplace." See Law Commission, Report on Bills of Sale (Law Com No 369, 2016) para 4.66.

[58] See the Debt Arrangement and Attachment (Scotland) Act 2002 ss 11, 45, 46 and 47 and sch 2.

[59] 2002 Act s 11(1)(b).

[60] Mr Roddy Macpherson.

instruments would also be of interest to secured creditors. Another possibility would be an art work.

19.43 There is, however, a disadvantage to the threshold-figure approach, of which we were aware, but which was also highlighted to us by Professor Hugh Beale and Professor Louise Gullifer in their response to our draft Bill consultation of July 2017. Sometimes assets form part of a collection, for example books and stamps. The individual items may be worth less than the threshold figure but collectively they may significantly exceed it. But trying to frame an appropriate rule which would catch certain collections but not others, for example furniture and toys, would take us back to a list-approach with the problems outlined earlier.

19.44 A third approach favoured by the New Zealand Law Commission and now implemented by legislation is to draw up a clearer and shorter list than the one currently found in the 2002 Act.[61] Such an approach is an entirely reasonable one but the relatively short New Zealand list applies to security rights under consumer contracts in general and thus also applies to hire-purchase. Our rule would only apply to the statutory pledge. Given the views of consultees that a wider range of assets should be excluded from the scope of the statutory pledge, on balance we recommend a rule preventing the security right being granted over items below a certain prescribed value.

19.45 In relation to such a rule it must be clear whether the threshold value is to be ascertained at the time of the grant of the statutory pledge or at the time of enforcement. For diligence under the 2002 Act it is obviously the value at enforcement which matters, as diligence is not granted.[62] There are arguments both ways. It is easier to value an asset at the present time than to ascertain its historic value at the time of grant. On the other hand, a rule requiring value above a certain level to permit enforcement might encourage dishonest debtors to devalue the asset. On balance we think that the value should be at the time of grant.

19.46 We further consider that the restriction should only apply to corporeal assets. Later we recommend that the statutory pledge should be restricted for the time being to financial instruments and intellectual property.[63] Neither of these can be regarded as essential domestic assets and they are not property which is exempted from diligence.

19.47 There was no support from consultees for the suggestion that for consumers the statutory pledge should only be available for purchase finance. We concluded above that it

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[61] See Law Commission of New Zealand in its *Consumers and Repossession* (Report 124, 2012) paras 3.38-3.72 which considers (1) a prohibition on granting security over household goods, including cars up to the value of NZ$5,000 (about £2,500) and (2) a "protected goods list". On balance (at para 3.42) it favoured the latter, with the list to be prescribed by statutory instrument: "From the debtor's perspective, as many submissions commented, there is a risk that if too wide a category of goods were to be exempted from repossession or a blanket prohibition on repossession of goods below a particular value imposed, some would be prevented from accessing credit. From an economic perspective, there would also be the fear that this might prevent poorer people from being able to use whatever limited equity they have to finance credit. Overly paternalistic legislation risks undermining the interests of those it seeks to protect." At para 3.50 it recommends that medical equipment, bedding, portable heaters, stoves, washing machines and cooking equipment are on the protected goods list, but not televisions and cars. The recommendations were implemented by the Credit Contracts and Consumer Amendment Act 2014 s 51, inserting a new s 83ZN to the Credit Contracts and Consumer Finance Act 2003.

[62] With the arguable exception of the right to carry out summary diligence.

[63] See Chapter 22 below.

should not be possible for consumers to grant the statutory pledge over future assets.[64] The DCFR does, however, allow security to be granted over a future asset to secure repayment of sums advanced to help acquire the asset in question.[65] Thus Brian could grant a security right over a specific car which he is in the process of acquiring in order to secure a loan that he has received from a bank towards the purchase. Such a security right, in the language of UCC–9 and the PPSAs, is a PMSI (purchase money security interest). The alternative is to have an unqualified restriction on the statutory pledge being granted over future goods. This would mean that Brian could in principle only grant the statutory pledge over the car to the bank once he became owner, although the common law doctrine of accretion would arguably apply. As the parameters of that doctrine, not least in relation to moveable property are unclear,[66] we think that it would be preferable to have an express rule along the lines of the DCFR provision. We note also that the Law Commission for England and Wales has recommended a similar approach for goods mortgages, its recommended replacement for bills of sale, which would be available for consumers.[67]

19.48 Finally, the DCFR also has a rule that where a consumer grants a security right over moveables the assets to be encumbered must be identified individually.[68] Thus it is impermissible to grant a security right over "my vehicles" or "my computers". Drobnig and Böger in their commentary on the provision note:

> "While this requirement in certain cases may be time-consuming and therefore may even increase the expenses of contracting, still it is a useful way of avoiding surprise and raising awareness of the risks which the consumer security provider may incur in case of non-performance of the obligation to the secured creditor."[69]

19.49 Similarly the Law Commission for England and Wales recommended in its Consultation Paper on Registration of Security Interests: Company Charges and Property other than Land:

> ''(t)he need to hand the property over to the pawnbroker is likely to bring home to the consumer the significance of what she is doing and the risk that, if she defaults in payment, the property may be lost. We think this 'cautionary' function is important but we also think that it would be possible to build sufficient safeguards into any notice-filing system. . . In particular, we consider that it would be possible for consumers to be permitted to create security interests over their existing personal property if the items concerned are individually listed in the security agreement (and, in this context, a description along the lines of 'all existing property' should not be sufficient)."[70]

19.50 We therefore consider that where a consumer grants a statutory pledge it should be a requirement that the property to be encumbered is specifically identified in the constitutive

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[64] See para 19.38 above.
[65] DCFR IX.–2:107(1)(b).
[66] See Anderson, *Assignation* paras 11-46–11-52. See also paras 5.88–5.92 and 5.99–5.100 above.
[67] Law Com No 369, 2016 paras 4.68–4.73. The Report is to be implemented by a Goods Mortgages Bill, announced in the 2017 Queen's Speech.
[68] DCFR IX.–2:107(1)(a).
[69] Drobnig and Böger, *Proprietary Security in Movable Assets* 295.
[70] Law Com CP No 164, 2002 para 10.31. See too the Law Commission of New Zealand in its *Consumers and Repossession* (Report 124, 2012) paras 3.17-3.22 implemented by the Credit Contracts and Consumer Amendment Act 2014 s 51, inserting a new s 83ZF to the Credit Contracts and Consumer Finance Act 2003.

document of the statutory pledge (or if relevant an amendment document adding property to the statutory pledge).[71]

19.51 Our recommendations can be set out as follows. We use the term "individual" to mean "consumer" and we discuss how that term should be defined in the following paragraphs.[72]

> **78. (a) Where the provider of a statutory pledge is an individual the encumbered property should require to consist only of assets separately identified in the constitutive document (or in any amendment document) and which are either:**
>
> **(i) the provider's property at the time that document is granted, or**
>
> **(ii) acquired by the provider after that time if the acquisition is financed by credit and an obligation to repay that credit is the secured obligation.**
>
> **(b) A corporeal asset so identified should require, immediately before that document is granted, to have a monetary value exceeding £1,000 or such other prescribed amount.**
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> (Draft Bill, s 52(1) to (3))

What is a consumer?

19.52 The Consumer Credit Act 1974 uses the term "individual" to refer to consumers. That term is defined more widely than might be expected as including:

> "(a) a partnership consisting of two or three persons not all of whom are bodies corporate; and
>
> (b) an unincorporated body of persons which does not consist entirely of bodies corporate and is not a partnership."[73]

Certain credit agreements made with individuals are, nevertheless, outwith the scope of the 1974 Act, notably loans of more than £25,000 taken out for business purposes and loans of more than £60,260 to high net worth individuals.[74]

19.53 In contrast the Consumer Rights Act 2015 defines a "consumer" more narrowly as "an individual acting for purposes that are wholly or mainly outside that individual's trade,

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[71] On constitutive document and amendment documents, see Chapter 23 below.
[72] See paras 19.52–19.55 below.
[73] Consumer Credit Act 1974 s 189(1). For discussion, see W C H Ervine, *Consumer Law in Scotland* (5th edn, 2015) para 8-35.
[74] Consumer Credit Act 1974 s 8 and the Financial Services and Markets Act 2000 (Regulated Activities) Order 2000 (SI 2001/544) arts 60C and 60H. In broad terms, individuals are considered to be of "high net worth" if they have a net income of £150,000 or more, or assets of £500,000 or more (not including a home or pension). For this exception to apply, the debtor must make a declaration agreeing not to have the usual protections and obtain a statement from an accountant providing details of their income or assets. See Law Commission, Bills of Sale (Law Com CP No 22, 2015) para 4.13.

business, craft or profession."[75] Similarly, the DCFR provides that a consumer is "any natural person who is acting primarily for purposes which are not related to his or her trade, business or profession."[76] Likewise, the New Zealand Credit Contracts and Consumer Finance Act 2003 limits a consumer credit contract to where the debtor is a natural person and the credit is to be "used, or is intended to be used, wholly or predominantly for personal, domestic, or household purposes".[77]

19.54 The question is how widely the consumer protection recommendations set out in the paragraphs above should be applied. In other words, how broadly should "individual" be defined? Following reflection we consider that "individual" should be given its ordinary meaning of "natural person". We are not convinced that the broader definition in the 1974 Act is apposite. Sole traders or small partnerships should not, we believe, have to identify specifically business assets when granting a statutory pledge or be restricted from granting it over low-value property such as tools or equipment which collectively may be worth thousands of pounds and therefore may be of interest to a prospective lender. We think that such an approach would restrict access to business finance. Our advisory group agreed. Therefore, while the protections should apply to individuals within the natural meaning of that word, they should not apply to sole traders in relation to assets used, or to be used, wholly or mainly for business purposes. Thus Peter, a sole trader plumber, would be able to grant a statutory pledge over equipment used by him for his business no matter the value of the individual items.

19.55 We recommend:

79. The restrictions on the grant of a statutory pledge in relation to individuals should not apply to sole traders as respects any assets used, or to be used, wholly or mainly for the purposes of that sole trader's business.

(Draft Bill, s 52(4))

Moveable property

19.56 The possessory pledge is restricted to moveable property.[78] The statutory pledge too would be a security over moveable property. For immoveable (heritable) property the appropriate security is the standard security.[79] In the Discussion Paper we noted that UCC–9 and some of the PPSAs provide for personal property security interests to extend to "fixtures", that is moveables that have become part of immoveable property by accession.[80] But other PPSAs, notably New Zealand, have not followed this approach. We expressed the view that we too should not follow it, because it results in complexity whereby assets are subject simultaneously to land law and to the statutory pledge regime. We asked consultees if they agreed.

[75] Consumer Rights Act 2015 s 2(3).
[76] DCFR I.–1:105(1).
[77] Credit Contracts and Consumer Finance Act 2003 s 11(1)(a) and (b).
[78] Steven, *Pledge and Lien* ch 5.
[79] Our future project on heritable securities will consider reform of the standard security.
[80] Discussion Paper, para 16.49.

19.57 Consultees generally agreed. These included Brodies, the Faculty of Advocates, the Judges of the Court of Session and the Law Society of Scotland. Scott Wortley said that "permitting moveable securities to cover heritable property would cause potential problems for conveyancing practice." But Professor Eric Dirix suggested that any conflict between a statutory pledge and a standard security over the same property could be decided by reference to the date of registration.

19.58 Several consultees raised wider questions in relation to the law of accession. For example, ABFA and the WS Society mentioned the desirability of clarifying the law on accession of one corporeal moveable to another corporeal moveable.[81] While we see the force of this it goes beyond the scope of this project. As Dr Hamish Patrick noted: "any alternative [to the approach proposed] really requires reconsideration of the law of fixtures and various other issues relating to heritable property rights". The Law Society of Scotland appreciated that some of the wider issues may "more properly be considered in the context of the many vexed questions which arise in commercial practice under the law of accession of moveables to land and the law of fixtures."

19.59 Brodies sought clarification on the issue of "whether . . . temporary accession and subsequent separation of the moveable property from heritable property should have the effect of defeating the new moveable security." Assuming that accession has actually occurred the statutory pledge would indeed be defeated because it is only capable of covering moveable property. However, if the property was subsequently separated and the statutory pledge was granted over both present and future assets,[82] it could become subject to the security right again.

19.60 We recommend:

80. It should be competent to grant a statutory pledge over moveable property but not over property that has acceded to immoveable (heritable) property.

(Draft Bill, s 43(1))

Corporeal and incorporeal property

19.61 Moveable property divides into corporeal moveable property and incorporeal moveable property. The former has a physical presence, the latter does not. We deal with the two different types of moveable property in Chapters 21 and 22 below.

Transferability

19.62 For both possessory and statutory pledges the encumbered property should require to be transferable.[83] A pledge ultimately needs to be enforceable by realising the asset – normally by selling it – and that is effectively precluded if it is non-transferable. For

[81] On which, see Reid, *Property* paras 588–591.
[82] On the ability of the statutory pledge to cover future assets, see the next chapter.
[83] See eg the Belgian Pledge Act of 11 July 2013 art 12 (which provides for art 7 of the new Book III title XVII of the Civil Code).

possessory pledge there is case law that companies cannot encumber their Register of Shareholders[84] or letters of guarantee.[85]

19.63 For the statutory pledge, certain intellectual property licences may have restrictions on their transfer and we also mention this issue in Chapter 22. We consider that as long as the property is transferable, even if there are restrictions on that transferability, it should be capable of having a pledge granted over it.[86]

19.64 We recommend:

81. The encumbered property should require to be transferable (whether or not its transferability is restricted in some way).

(Draft Bill, s 44(4))

Proceeds and fruits

19.65 A general feature of UCC–9 and the PPSAs is that where the debtor sells the collateral, the proceeds of sale (and of insurance policies for fire loss etc) are automatically subjected to the security interest.[87] The Murray Report, however, rejected this approach.[88] We too rejected it in the Discussion Paper.[89] Partly this was for the reason that proceeds rules are complex and add very considerably to the complexity of legislation on secured transactions law arguably without sufficient countervailing benefits. Our other reason was that if the new security were permitted to cover after-acquired assets then it could cover proceeds too, not by virtue of a special rule, but simply by virtue of the scope of the security right. Thus if a provider granted the new security over its stock and receivables, and an item of stock was sold on credit, the receivable that arose because of the sale would be covered.

19.66 A clear majority of our consultees agreed with us. Brodies and the Law Society of Scotland considered this "likely to be the only practicable solution". Other law firm consultees expressed a similar view. Dr Ross Anderson stated that "The English law on proceeds is a warning sign to undesirable sophistry." In contrast Jim McLean considered a proceeds rule to be "indispensable". Professor Eric Dirix recommended one. Professor Hugh Beale argued that secured creditors would expect such a rule in order to protect them against unauthorised transfers, where the transferee obtained an unencumbered title under good faith acquisition rules.[90]

19.67 For reasons explained later,[91] we recommend that the statutory pledge should not be available in respect of receivables. This policy change removes the argument that a

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[84] *Liquidator of Garpel Haematite Co Ltd v Andrew* (1866) 4 M 617.
[85] *Robertson v British Linen Co* (1890) 18 R 1225.
[86] For an alternative approach, see the Security Interests (Jersey) Law 2012 s 1 definition of "intangible movable property" as including "licences and quotas having commercial value, whether or not they are transferable". The idea is that while a licence or quota in principle cannot be transferred the relevant authority issuing it may be willing to agree to its transfer. See the Canadian case of *Saulnier v Royal Bank of Canada* [2008] 3 SCR 166, discussed in R M Goode, *Principles of Corporate Insolvency Law* (4th edn, 2011) para 6-11. But the statutory pledge would not, at least initially, be available in respect of these types of property.
[87] UCC-9-203(f); DCFR IX.–2:306.
[88] Murray Report para 3.5; Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 9(3).
[89] Discussion Paper, para 16.48.
[90] See H Beale, "A View from England" (2012) EdinLR 278 at 280. On good faith acquisition, see Chapter 24 below.
[91] See paras 22.5–22.18 below.

statutory pledge could cover proceeds by express provision. Nevertheless, there are other ways in which proceeds could be encumbered. Where the provider of a statutory pledge is a company, the likelihood is that a floating charge will be granted at the same time. It can extend to proceeds, a point noted by some of our consultees.[92] Another possibility is for proceeds to be expressly assigned in security by means of registration in the Register of Assignations under our recommendations elsewhere.[93]

19.68 We remain of the view that proceeds rules are complex and of course under UCC–9 and the PPSAs they are generic to all security rights over moveables. Our recommendations are far more limited. The law on proceeds is arguably best considered in relation to the law of rights in security as a whole, which is clearly beyond our scope. Accordingly, we do not recommend a general proceeds rule.

19.69 Nevertheless, we consider that there would be benefit in setting out default rules in relation to the narrower subject of fruits. It appears to be the case that a possessory pledge of corporeal moveables covers natural fruits.[94] Thus a pledge of sheep will include any subsequently-born lambs. We think that this should be the default rule for statutory pledges too.

19.70 In contrast, for incorporeal (civil) fruits such as dividends on shares of a company or income derived from a licence of intellectual property, the default rule should be that these are not included. When security is granted over shares the parties normally want things to continue as they are, unless and until there is enforcement. Thus the provider (who remains the shareholder as the statutory pledge is a true security right) should remain entitled to the dividends and likewise in relation to any royalties on a patent. For the reasons discussed below,[95] the statutory pledge is to be restricted to financial instruments and intellectual property. There is therefore an argument that incorporeal fruits such as dividends, not being financial instruments or intellectual property, must be outwith the scope of the statutory pledge in any event. Our view, however, is that as fruits it should be possible for these to be included if the parties so provided. But the default rule would be that these are excluded. We recommend:

19.71 We recommend:

82. The encumbered property should (except in so far as the provider and the secured creditor agree otherwise) include the natural fruits, but not the incorporeal fruits, of the property.

(Draft Bill, s 44(3)(b))

Construction contracts

19.72 In the Discussion Paper we raised the issue of whether any special regime would be needed as regards the application of the new security right to construction contracts.[96] Sub-contractors are subject to the risk of insolvency of the main contractor occurring at a time

[92] Admittedly floating charges have a lower ranking than fixed securities such as the statutory pledge.
[93] See volume 1 of this Report.
[94] Steven, *Pledge and Lien* para 8-01. This does not mean that the secured creditor can generally appropriate them for that party's own benefit. See Steven, *Pledge and Lien* para 7-10.
[95] See Chapter 22 below.
[96] Discussion Paper, para 18.24.

when sums are owing to the sub-contractor. We considered that sub-contractors could protect themselves by having the main contractor grant security over the sums due from the employer.[97] Of course the main contractor might not be willing to oblige but the facility would be there. Consultees were almost unanimous in not seeing the need for any special regime here. Aberdeen Law School doubted whether sub-contractors could demand the grant of the security in a marketplace where there are several tenderers. We recommend therefore:

83. There should not be a special regime for construction contracts.

[97] We suggested that the new security could be granted over the sums. For the reasons explained in Chapter 22 below we are recommending that the statutory pledge should not, at least initially, be available in respect of sums, but assignation in security completed by registration would be available. The general point therefore continues to hold.

Chapter 20 The statutory pledge: a fixed security

Introduction

20.1 English law recognises security rights known as "charges".[1] There are two types: "fixed charges" and "floating charges". In respect of corporeal moveables (chattels), both are non-possessory. Scottish common law recognises neither, but of course floating charges were introduced by statute in 1961.[2] Only companies, LLPs and a limited number of other entities can grant floating charges. As a result of their introduction the concept of a "fixed security" established itself in legislation on floating charges in Scotland.[3] Further, it is an important feature of corporate insolvency which applies throughout the UK.[4]

20.2 But the current law is very restrictive as to fixed securities over moveable property in Scotland. The only one generally available[5] is the possessory pledge. It is limited to corporeals and requires delivery to the secured creditor. As we have discussed elsewhere,[6] to take security over incorporeals the only option currently available is to transfer the asset to the creditor. For completeness, we note that when a floating charge is enforced so that it "attaches" to the property of the company or other entity, it becomes a "fixed security".[7]

20.3 The Scottish courts have unsurprisingly struggled with the fixed/floating distinction.[8] In English law the situation is hardly better. The landmark House of Lords decision in *National Westminster Bank plc v Spectrum Plus Ltd*[9] departed from previous authority and prompted a volume of essays.[10] A Discussion Paper published by the Financial Law Committee of the City of London Law Society in 2012 describes the fixed/floating distinction as "a running sore in our legal system".[11]

20.4 The broad difference between a fixed charge/security and floating charge is that only with the latter is the provider free to deal with the encumbered property without the consent of the secured creditor. To put it another way, where a floating charge has been granted, the secured creditor does not have "control" of the assets. Thus a retail business which

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[1] See eg Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* paras 6.93–6.139 and Calnan, *Taking Security* chs 3 and 4.
[2] See paras 17.29–17.40 above.
[3] See in particular the Companies Act 1985 ss 464 and 486(1).
[4] See in particular the Insolvency Act 1986 ss 53(7), 54(6), 55(3), 60(1) and 70(1).
[5] In addition there are some specialist security rights, notably aircraft mortgages and ship mortgages.
[6] See para 17.5 above.
[7] Companies Act 1985 s 463, Insolvency Act 1986 ss 53(7) and 54(6). See *National Commercial Bank of Scotland Ltd v Liquidators of Telford Grier Mackay & Co* 1969 SC 181. But floating charges now are generally enforced by the appointment of an administrator. On this see D Cabrelli, "The curious case of the 'unreal' floating charge" 2005 SLT (News) 127.
[8] See eg *Cumberland Development Corporation v Mustone Ltd* 1983 SLT (Sh Ct) 55, criticised in G L Gretton, "Receivership and Sequestration for Rent" 1983 SLT (News) 277.
[9] [2005] UKHL 41, [2005] 2 AC 680.
[10] J Getzler and J Payne (eds), *Company Charges: Spectrum and Beyond* (2006).
[11] City of London Law Society Financial Law Committee, Discussion Paper: Secured Transactions Reform (2012) para 4.24 available at http://www.citysolicitors.org.uk/attachments/article/121/20121120-Secured-Transactions-Reform---discussion-paper.pdf.

grants a floating charge over all its assets including its stock-in-trade does not need the secured creditor's involvement to sell the stock to purchasers and give them an unencumbered title. On the sale, the asset simply escapes from the scope of the charge. If the provider, however, becomes insolvent the charge "crystallises" and becomes a fixed security, at which point the assets can no longer be dealt with freely.

20.5 In contrast, where there is a fixed charge/security the creditor's involvement is needed to disencumber an encumbered asset if the debtor sells it. For example, Anna pledges her watch to Ben in security of a loan. As is required by the current law of pledge, Ben must be given possession of the watch. But this does not prevent Anna selling the watch to Carol. Nevertheless, Carol takes the watch encumbered by the pledge. To disencumber the watch requires Ben's consent.

20.6 Two further points should be mentioned about the difference between fixed charges/securities and floating charges. First, the need for the creditor to release the security in order for a purchaser to acquire an unencumbered title makes fixed security unsuitable for assets which a business needs to deal with freely such as stock-in-trade. Thus fixed securities are granted over narrower classes of assets. Secondly, fixed securities have a higher ranking in insolvency than floating charges. Floating charges are postponed to (a) preferential creditors (mainly employees for wages);[12] (b) the "prescribed part" (a carve-out for unsecured creditors);[13] and (c) the expenses of an administration.[14] Fixed charges/securities are not.

Discussion Paper

20.7 The approach taken in the Discussion Paper was that the new security right should have both a fixed and a floating version. The fixed version would fill a huge void in the current law. But how would the floating version compare to the floating charge? We provisionally labelled this version the "floating lien"[15] and argued that it would have a "superior inner logic"[16] when compared with the floating charge. We conjectured that if the banks began to use the floating lien then the floating charge would "fade away in practice".[17]

20.8 The Discussion Paper, nevertheless, recognised the support for the floating charge among financial institutions in Scotland. It asked therefore: "Do consultees agree that the floating charge should not be abolished, at least for the time being?"[18] This question drew the most passionate responses in the entire consultation. The Law Society of Scotland stated that it was "strongly against any move to abolish floating charges". Two major law firms[19] said: "We strongly oppose the proposal to abolish floating charges". ICAS/R3 commented that the Discussion Paper "briefly suggests abolishing the floating charge in its current form." It continued: "We would be concerned that this would put Scotland at a commercial disadvantage to other parts of the UK." These responses demonstrate a strong level of support for the floating charge, even with the conceptual problems it has created for

[12] Insolvency Act 1986 s 59.
[13] Insolvency Act 1986 s 176A.
[14] Insolvency Act 1986 Sch B1 para 99(3).
[15] Discussion Paper, Chapter 22.
[16] Discussion Paper, para 22.22.
[17] Discussion Paper, para 22.28.
[18] Discussion Paper, para 22.28.
[19] Dundas & Wilson and McGrigors.

Scottish law which we have discussed elsewhere.[20] In another part of their response to the Discussion Paper, Dundas & Wilson stated: "We strongly believe that steps to replace the floating charge with a system that differs from that currently existing will be retrograde. The system as currently operated is entrenched and works extremely well in practice."

20.9 Moreover, some of the responses criticised the idea of introducing a new floating security as in effect duplicating the floating charge. McGrigors stated: "The [Discussion Paper] appears in certain areas to propose a "floating lien" which seems to be a floating charge by another name, and have limited utility." Dr Hamish Patrick said: "Distinguishing a category of new security as a "floating lien" is misconceived. If a given new (or existing form) security includes future assets and permits disposal of existing and future encumbered assets it is likely to be treated as if it were a floating charge for the purposes of insolvency legislation." Comments were made to similar effect at the symposium which we held at the University of Edinburgh in October 2011.[21]

20.10 One of the main rationales set out in the Discussion Paper for the "floating lien" was so that the new security right could cover future property. We said:

> "On balance we think that the floating lien should be introduced, or, to put the point more correctly, we think that the new security right that we propose should not be limited to present assets."[22]

20.11 This, however, overlooked the fact that in English law fixed (as well as floating) charges can attach to future assets. In the words of a leading text:

> "There is little doubt that the mere fact that the charge covers both present and future assets does not prevent it being a fixed charge. The power to add assets to those charged is not inconsistent with a fixed charge. This is hardly surprising. Future assets can be identified with as much specificity as current assets, and, when they come into existence, the charge can attach to them in the same way as it attaches to existing assets."[23]

20.12 While some might wish to qualify the first part of the final sentence, the general proposition holds that a fixed charge may be granted over future property. Thus Magdalena Raczynska commented in her consultation response: "I think that it is possible to conceptualise fixed security as security over future assets as well as present so long as they are identified in the contract or are a result of authorised dispositions of the collateral by the debtor."

20.13 This point was also made by a number of contributors at the University symposium, notably by Professor Hugh Beale.[24] As Professor George Gretton subsequently noted:

> "[M]ore than one speaker pointed out that the Discussion Paper imperfectly identifies the concept of "floating". This concept was adopted into the insolvency legislation on corporate insolvency from English law, but without explanation, so that a Scots

[20] See para 17.35 above.
[21] The papers presented at that symposium are published at (2012) 2 Edin LR 261.
[22] Discussion Paper, para 22.22.
[23] Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 6.97.
[24] And see H Beale, "A View from England" (2012) 16 Edin LR 278 at 279.

lawyer has to work it out from English law. The key point is not "floating in" but "floating out"."[25]

20.14 Consultees also commented that there needed to be clarity as to when the new security right would be treated as fixed and when it would be treated as floating for the purposes of corporate insolvency legislation. More broadly, however, there was strong support from consultees for the proposition that the new security right should not be limited to present assets (other than in consumer cases).[26] We agree that the statutory pledge should be able to be granted over future property and we discuss how it would actually be created in respect of such property in Chapter 23 below.

Fixed only

20.15 The fact that it would be possible for the new statutory pledge to be a fixed security in relation to future property removes some of the impetus for introducing the floating lien. But we consider now that there are other reasons for not doing so.

20.16 In practical terms perhaps the main difference between the floating lien proposed in the Discussion Paper and the floating charge is that the former should be capable of being granted not just by companies, LLPs etc but by any person, excluding consumers. Thus sole traders and partnerships would be able to grant it. On reflection we now have two significant doubts about recommending a floating lien which sole traders and partnerships could grant.

20.17 First, in our consultation we received no compelling evidence that the inability of non-corporate businesses to grant a floating charge as opposed to fixed security was inhibiting access to loan finance.

20.18 Secondly, in the insolvency of companies and LLPs etc, unsecured creditors receive some priority over floating charges as a result of (1) the preferential creditor rules for employees etc and (2) the prescribed part.[27] It was accepted in the Discussion Paper[28] and consultees generally agreed that the same rules would have to apply where a company or LLP etc granted a floating lien. But the prescribed part has no parallels in sequestration, which is the insolvency process for sole traders and partnerships. While there is protection for preferential creditors in schedule 3 of the Bankruptcy (Scotland) Act 2016, such creditors rank below secured creditors in a sequestration. We are concerned therefore about the position of unsecured creditors in this context if there were to be a new "floating" security. One solution of course would be to recommend an amendment to insolvency law, but this is in principle outwith the scope of this Report.

20.19 In contrast, there are no such difficulties with insolvency law in relation to a new fixed security right, because fixed securities rank ahead of preferential creditors and the prescribed part.[29] In fact, the effect of introducing a fixed security over moveables in Scotland would be to create a level playing field north and south of the Scotland/England border. As we noted earlier in this Report,[30] the WS Society said that reform in this area

[25] G L Gretton, "Reform of Security over Moveable Property" (2012) 16 Edin LR 261 at 265 fn 10.
[26] Discussion Paper, para 22.22. On consumer protection see paras 19.36–19.55 above.
[27] See para 20.6 above.
[28] Discussion Paper, paras 22.16–22.19.
[29] See para 20.6 above.
[30] See para 1.15 above.

should be the first priority for the Commission as there was "no workable fixed security in Scots law."

20.20 We mentioned above that the Discussion Paper suggested that the introduction of the floating lien could mean that the floating charge would fade away.[31] On reflection we think that there are at least two reasons why this is unlikely. The first is the ongoing use of floating charges in England and Wales, with which banks and their lawyers are familiar. We recounted earlier the fate of Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007 which sought to put Scottish floating charges law on a separate footing but which has never been brought into force due to stakeholder opposition.[32] In his response to the Discussion Paper, Jim McLean stated: "Floating liens should not be introduced in Scotland alone, so long as the floating charge continues to exist elsewhere in the UK." Brodies noted: "Despite the conceptual issues associated with floating charges our view is that they do nevertheless have their uses benefiting lenders (an arguably enhanced security package and certainly enhanced enforcement mechanism) and for the customer the ability to grant a security package on similar if not entirely consistent terms with other jurisdictions within the UK."

20.21 There may well be reform of the fixed/floating distinction in England and Wales. The Financial Law Committee of the City of London Law Society published a Discussion Paper on the subject in 2014.[33] And the Secured Transactions Law Reform Project published its own Discussion Paper in 2017.[34] Until there is such reform we expect that the floating charge would continue to be the preferred floating security right even were a floating lien to be introduced in Scotland.

20.22 The second reason is that the floating charge can encumber land. The floating lien would only cover moveables. We understand that the ability of the floating charge to attach to land is popular among the banks, not least because of the current enforcement rules on standard securities. The Law Society of Scotland said in its response to our Discussion Paper: "[We are] of the view that if the floating lien is to have many of the characteristics of a floating charge, it will not be attractive, not least since the proposed floating lien will not have the benefits of (i) being a truly universal security (covering heritable assets as well as moveables); and (ii) not providing the same control, viz, the right to appoint an administrator."[35]

20.23 We conclude that the priority is to introduce a new fixed security over moveable property in Scotland. We refer to the comments of two major law firm consultees[36] in response to the Discussion Paper:

> "[W]e share the widely held view that the fundamental need at the moment is to create a non-possessory form of *fixed* security: a practical, effective and widely

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[31] See para 20.7 above.
[32] See paras 18.23–18.25 and 18.41–18.43 above.
[33] The discussion paper is available at http://www.citysolicitors.org.uk/attachments/article/121/20140219%20Secured%20Transactions%20Reform%20Discussion%20Paper%202%20Fixed%20and%20floating%20charges%20v2.pdf.
[34] The discussion paper is available at https://stlrp.files.wordpress.com/2017/01/paterson-fixed-and-floating-charges.pdf. The author is Professor Sarah Paterson.
[35] See also the City of London Law Society Financial Law Committee, Draft Secured Transactions Code and Commentary (2016) section 11 (pp 41–43) available at http://www.citysolicitors.org.uk/attachments/article/121/Draft%20Secured%20Transaction%20Code%20-%20Commentary%20-%20July%202016.pdf.
[36] Dundas & Wilson, and McGrigors.

accepted form of floating security is available and used under the floating charge regime which we believe is perfectly workable and acceptable."

20.24 While we continue to have reservations about the law on floating charges and we consider this type of security right further in Chapter 38 below, there is clearly little appetite amongst stakeholders at the present time for the floating lien. Our advisory group agrees that the best way forward is for the statutory pledge to be a fixed security only. Nevertheless, developments in England and Wales, in relation to both secured transactions law and corporate insolvency law in the future may cause the position to be reconsidered.

20.25 There is further advantage in making the statutory pledge fixed only because it makes our new legislative scheme simpler. We have noted elsewhere that previous attempts to reform the law of security over moveables have foundered because they have been too ambitious.[37] It also means that some of the questions which we asked in the Discussion Paper are now superseded.[38]

20.26 We recommend:

84. (a) The statutory pledge should be a fixed security only.

(b) The definitions of "fixed security" in the Companies Act 1985 and the Insolvency Act 1986 should be amended to include reference to the statutory pledge.

(Draft Bill, s 65)

Requirements for the statutory pledge as a fixed security

General

20.27 In order to be a fixed security there require to be restrictions on the ability of the provider to deal with the property which is subject to a statutory pledge. The Murray Report accepted this in relation to the new "moveable security" which it proposed. Its draft Bill had a clause dealing with the matter.[39] The commentary on that clause notes that it "provides the rule that the granter of a moveable security may not dispose of or assign property which is subject to that security, without the prior, written consent of the holder of the security. This rule reflects the nature of the moveable security as a fixed security over moveable property (as distinct from a floating charge)."[40]

20.28 In the leading English case of *National Westminster Bank plc v Spectrum Plus Ltd*,[41] Lord Scott of Foscote sought to distinguish fixed and floating charges:

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[37] See para 18.33 above.
[38] In particular, questions 81 (Do consultees agree that if the floating lien is introduced, it would have to be treated, for the purposes of insolvency law, in substantially the same way as the floating charge?), 82 (Specifically, should the special rule in section 245 of the Insolvency Act 1986 apply to the new security, to the extent that the collateral in question had been acquired by the debtor after the registration of the security?) and 83 (If the floating lien is introduced, should it be subject to the "effectually executed diligence" rule?).
[39] Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 11.
[40] Murray Report "Notes on Clauses" 9.
[41] [2005] UKHL 41.

> "In my opinion, the essential characteristic of a floating charge, the characteristic that distinguishes it from a fixed charge, is that the asset subject to the charge is not finally appropriated as a security for the payment of the debt until the occurrence of some future event. In the meantime the chargor is left free to use the charged asset and to remove it from the security."[42]

20.29 It is the chargor's (provider's) freedom to remove the property from the scope of the charge which is the fundamental requirement, as making ordinary use of the property is not inconsistent with the charge being fixed.[43] Richard Calnan puts it as follows:

> "In theory, the distinction between fixed and floating charges is straightforward. The only difference is that a debtor which has created a floating charge has a prospective general authority to deal with its assets free from the charge before crystallisation, whereas a debtor which has created a fixed charge requires the specific authority of the creditor each time it wishes to deal with the asset concerned."[44]

20.30 Increasingly, the need for the secured creditor to give consent to dealings with the encumbered property has come to be viewed in terms of that creditor having "control" of that property.[45] This is particularly true in relation to the vexed issue of charges over receivables and their proceeds.

20.31 Back in 1979 in *Siebe Gorman & Co v Barclays Bank*[46] it was held sufficient to create a fixed charge over receivables by stating in the charge document that the charge was fixed and requiring the proceeds to be paid into an account with the bank which was the secured creditor. The provider was otherwise free to deal with the proceeds. In *Re New Bullas Trading Ltd*[47] an approach was approved whereby the charge document purported to create a fixed charge over receivables but a floating charge over their proceeds, in respect of which there was freedom to deal.

20.32 More recently, the courts have taken a noticeably stricter approach to freedom to deal. The Privy Council in an appeal from New Zealand in *Agnew v Commissioner for Inland Revenue*[48] concluded that *Re New Bullas Trading Ltd* had been incorrectly decided and that in such circumstances only a floating charge was created. Then came the landmark decision in *National Westminster Bank plc v Spectrum Plus Ltd*,[49] which overruled *Siebe Gorman.* The result is that the label used by the parties in the charge document to describe the charge cannot be definitive.[50]

20.33 To achieve a fixed charge now would seem to require a general prohibition on any dealing with regard to the encumbered property without the consent of the secured creditor.[51] Moreover, the secured creditor must be free to give or not to give consent. There must be a

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[42] [2005] UKHL 41 at para 111.
[43] Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 6.98.
[44] Calnan, *Taking Security* para 4.89.
[45] Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 6.106. Confusingly, the "control" required for a fixed charge is not synonymous with "control" under the Financial Collateral Arrangements (No. 2) Regulations 2003 (SI 2003/3226), on which see Chapter 14 above and Chapter 37 below.
[46] [1979] 2 Lloyd's Rep 142.
[47] [1994] BCC 36.
[48] [2001] UKPC 28, [2001] 2 AC 710.
[49] [2005] UKHL 41.
[50] See *Agnew v Commissioner of Inland Revenue* [2001] UKPC 28, [2001] 2 AC 710 at para 32 per Lord Millett.
[51] Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 6.107.

true discretion. Thus where the secured creditor is contractually obliged to consent to dealings the charge will be regarded as floating.[52]

Mandates to deal with the encumbered property

20.34 In the Discussion Paper we proposed that the secured creditor in the new security right should be able to authorise the provider to deal with the encumbered property free of the security on such terms and subject to such conditions as may be agreed.[53] We noted that this concept is sometimes known as "licence", but that a better juridical basis would appear to be mandate. We considered also that the general law of rights in security permits this. In response to our question as to whether consultees agreed that there was no reason why a creditor should not be able to mandate the debtor to deal with the collateral free of the security, most of the consultees were supportive.

20.35 We hold to the view that under the general law of rights in security such an arrangement is permissible. The difficulty, however, as we have seen in this chapter, is that corporate insolvency law in Scotland, following England and Wales, insists on a categorisation of "fixed securities" and "floating charges". Thus, Dr Hamish Patrick, while agreeing that a mandate to deal should be possible, noted that "distinctiveness from the floating charge is an issue here". Magdalena Raczynska, disagreeing with the question put to consultees, said: "I think this is destructive to the nature of security – the creditor loses the ability to resort to an asset in the event of the debtor's default. This is in my view the nature of a floating charge – that the grantor is able to deal away with property and as such should be governed by special rules."

20.36 We consider now that to allow a general mandate to deal would enable the statutory pledge to be tantamount to a floating charge and not compatible with it being a fixed security. In other words it should not be possible for the secured creditor to give the provider a blanket power to deal freely with the assets. Consent to a dealing should be required on a transaction by transaction basis, as discussed further below.[54] We recommend:

85. The secured creditor should not be able to give the provider a general mandate to deal with the encumbered property free of the statutory pledge.

Requirements for consent to dealing from secured creditor

20.37 In order to ensure that the statutory pledge satisfies the definition of a "fixed security" for the purposes of corporate insolvency law the indications from case law in England and Wales are that there must be fairly strict requirements for the consent which the secured creditor needs to give.[55] In other words, the secured creditor requires to have a relatively strong level of "control" over the property.

20.38 The Murray Report proposed that the sanction for breach of the relevant rules should be that the granter of the moveable security would be held to be in default.[56] For the

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[52] *Gray v G-T-P Group Ltd* [2010] EWHC 1772 (Ch).
[53] Discussion Paper, para 16.28.
[54] See paras 20.37–20.45 below.
[55] See para 20.33 above.
[56] Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 14(h).

statutory pledge the parties would be free to make express provision to the same effect, but we do not see a need to have this as an automatic rule. Rather, we consider that what is fundamental is that if the provider of a statutory pledge transfers the encumbered property (or any part of that property) to a third party other than with the appropriate consent, the encumbered property should remain encumbered by the pledge. This would, however, be subject to the rules which we discuss in Chapter 24 below under which certain good faith acquirers of the encumbered property would be protected.

20.39 We think that the consent should require to (a) be written; (b) refer to the particular transfer; (c) not include consent granted more than 14 days before the particular transfer; and (d) be at the discretion of the secured creditor.

20.40 In relation to (a), written consent could be given by means of pen and ink, or electronically (without an advanced electronic signature). We anticipate that an electronic communication would be normal.

20.41 In relation to (b), the consent would need to refer to a specific transfer to a specific person. Thus a consent to "any transfer of any of the encumbered property to a company in the same group as the provider" would not be sufficient as it refers only to a particular *transferee* rather than a particular transfer. The consent thus needs to be "positive". A "negative consent" provision under which the secured creditor is free to deal until such time, if any, that the secured creditor states otherwise, will not do.

20.42 In relation to (c), the requirement is for reasonable time proximity between the consent and the transfer. This means that it is unlikely to be effective for a consent provision to be inserted into the constitutive document of the statutory pledge. There will normally be a contract of sale between the provider and the third party. Under that contract transfer of ownership might be delayed for some time perhaps because of a retention of title clause.[57] In such circumstances it may be preferable for the secured creditor to grant a restriction,[58] because the time at which ownership is eventually to transfer may be unclear.

20.43 In relation to (d), as discussed above[59] there is authority in England and Wales that the secured creditor must have a true discretion and not be contractually bound to consent. Where encumbered property has been transferred without the required form of consent, it would be possible for the secured creditor to disencumber the property from the statutory pledge by means of a restriction or discharge.[60]

20.44 We are aware that the case law on "control" in English law has not been consistent over the years and that currently the requirements are more severe than they once were. It is not impossible that in the future judicial attitudes may change again. Another possibility is that UK corporate insolvency law is reformed. As we noted earlier,[61] the Financial Law Committee of the City of London Law Society and the Secured Transactions Law Reform Project have both published Discussion Papers on reform of the fixed/floating distinction.

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[57] Although this may not be the case because the secured creditor makes it a condition of consenting that the price is remitted to it forthwith. Therefore ownership transfers immediately, unless of course there is a retention of title clause for all sums and other sums which are owing.
[58] See paras 23.49–23.54 below.
[59] See para 20.33 above.
[60] See paras 23.49–23.54 below.
[61] See para 20.21 above.

With this in mind we think that it is sensible to give the Scottish Ministers power to amend the statutory provisions on consent in the draft Bill.

20.45 We recommend:

86. (a) If the provider of a statutory pledge transfers encumbered property to a third party other than with the consent mentioned below, the property should remain subject to the pledge.

(b) That consent should be the written consent of the secured creditor to the particular transfer and to the property in question being transferred unencumbered by the pledge, but should not include consent granted more than 14 days before the particular transfer.

(c) The granting or withholding of consent should require to be at the discretion of the secured creditor.

(d) The Scottish Ministers should have the power to make regulations amending the rules relating to consent.

(e) The foregoing recommendations should be subject to the recommendations made elsewhere as regards good faith acquirers.

(Draft Bill, s 53(1) to (3), (5) & (6))

Practical consequences

20.46 Since the statutory pledge is to be a fixed security this means that it would only be suitable for categories of assets with which the provider does not regularly deal. This is because obtaining creditor consent to disposals under the rules which we recommend above would limit the ability to transact. In particular, the statutory pledge would generally not be suitable for stock-in-trade (inventory). For that type of property the appropriate security right is a floating charge. Some examples may help.

20.47 Example 1. Ian is a florist. His main business assets are his flowers, vases, equipment (such as secateurs) and van. A statutory pledge would be a suitable security right as regards the equipment and van, as selling these assets is not a part of his normal trading activity. In contrast, the statutory pledge would not be appropriate for the flowers and vases as he needs to be able to sell these freely to customers.

20.48 Example 2. Maggieknockater Modern Motors Ltd is a motor dealership. Its main business assets are its office furniture, equipment and the vehicles which it buys and sells. A statutory pledge would be an appropriate security right in relation to the furniture and equipment, but not for the vehicles. As a limited company, Maggieknockater Modern Motors could grant a floating charge over all its assets including the vehicles, but as regards the furniture and equipment the statutory pledge as a fixed security would have a higher ranking.

20.49 Example 3. Colpy Combine Harvesters Ltd specialises in the sale of high value agricultural vehicles costing in excess of £100,000 each. While these are its stock-in-trade, on average it only sells a few a week and it takes some time for the sales paperwork to be agreed. It has a close working relationship with its bank. Here the statutory pledge may be

suitable on the basis of the bank consenting to individual sales.[62] Compared with Examples 1 and 2, the volume of disposals of the stock-in-trade is much lower.

20.50 Example 4. Whitehills Whisky Ltd is a wholesale whisky supplier. It exports whisky abroad. Its whisky is in numbered barrels and there are only a few exports every month. The statutory pledge could be possible here if a system can be set up whereby the secured creditor can authorise the release of particular barrels.

20.51 We are aware that by effectively excluding most stock-in-trade from the scope of the statutory pledge our recommendations would seem to run counter to one of the key objectives of an effective and efficient secured transactions law in the UNCITRAL Legislative Guide on Secured Transactions, namely validating non-possessory security rights in all types of assets.[63] It must be remembered, however, that for companies, LLPs and certain other corporate bodies the floating charge fulfils that role and that we had strong representations from consultees not to provide an alternative form of floating security. The UNCITRAL objective of course relates to secured transactions law in respect of moveable property[64] as a whole. As regards non-corporates, we have set out our reasoning above for making the statutory pledge a fixed security only.

Anti-avoidance

20.52 Finally, it seems necessary to have an anti-avoidance provision to prevent the statutory pledge being used *like a floating charge* in relation to stock-in-trade. In Chapter 24 below we recommend a rule whereby a good faith purchaser takes property unencumbered by a statutory pledge where the seller is acting in the course of a business. The situation therefore can be envisaged where Neil Ltd, a retailer, grants a statutory pledge over its stock-in-trade to Oswald. Neil Ltd's customers are protected because they are in good faith but Oswald gets the benefit of a fixed security over the stock-in-trade in the event of Neil Ltd's insolvency. But in practical terms the statutory pledge is functioning like a floating charge. We think that in such circumstances where the secured creditor is acquiescing in the provider dealing with the encumbered property without obtaining the proper consent to each disposal the statutory pledge should be extinguished.

20.53 We recommend:

> **87. A statutory pledge should be extinguished if the secured creditor acquiesces, expressly or impliedly, in the provider's transfer of the encumbered property or any part of it to a third party other than with the consent required by the legislation.**
>
> (Draft Bill, s 53(4))

[62] This example was suggested to us by Donna McKenzie Skene.

[63] Available at https://www.uncitral.org/pdf/english/texts/security-lg/e/09-82670_Ebook-Guide_09-04-10English.pdf. See p 21.

[64] And thus not immoveable property (land).

Chapter 21 Corporeal moveable property

General

21.1 This chapter considers security over corporeal moveable property, with particular regard to money, ships, aircraft, spacecraft, rolling stock, and motor vehicles.

21.2 As was seen in Chapter 17 above, the current law in this area is very inadequate. Aside from the floating charge, which can only be granted by companies, LLPs and a limited number of other entities, the only true security right generally available is the possessory pledge. It demands possession to be held by the secured creditor and is thus generally impractical for assets such as equipment and vehicles where a business requires these to be able to trade.

21.3 Scotland lags behind many other jurisdictions in not permitting a non-possessory security over corporeal moveables which is publicised by registration.[1] The case for allowing a fixed non-possessory security right over such property seems irrefutable. Aside from the special cases discussed below, we therefore recommend:

88. It should be competent to create a statutory pledge over corporeal moveable property.

(Draft Bill, s 43(1), (2)(b) & (4))

21.4 As we discussed in Chapter 19 above, this would mean for corporeal moveable property the creation of a pledge would require either delivery (possessory pledge) or registration in the Register of Statutory Pledges (statutory pledge).[2]

21.5 We turn now to consider special types of corporeal moveable property.

Money

21.6 Money, when in the form of coins and banknotes, is corporeal moveable property.[3] But it raises special issues. For this reason, it is excluded from the definition of goods in the Sale of Goods Act 1979.[4] It has been suggested that money cannot be made the subject of a security right.[5] From this view we would dissent and refer to legislation elsewhere.[6] Nevertheless, we consider that money should be outwith the scope of our recommended legislative scheme both for the possessory pledge and statutory pledge. Its inclusion would complicate the enforcement rules because of the special nature of money. Equally, we

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[1] See Discussion Paper, Appendix B. Permitting non-possessory security rights is one of the core principles of the European Bank for Reconstruction and Development's Model Law on Secured Transactions and a key objective of the UNCITRAL Legislative Guide on Secured Transactions. See Discussion Paper Appendix A.

[2] For after-acquired property, registration would be a pre-requisite for creation but the right would not be created until the property was acquired. See paras 23.22–23.27 below.

[3] See *SME Reissue* Banking, Money and Commercial Paper (2000) para 143 (L D Crerar).

[4] Sale of Goods Act 1979 s 61(1).

[5] *SME Reissue* Banking, Money and Commercial Paper para 145.

[6] See eg NZ PPSA 1999 s 16(1) (definition of "personal property").

consider it highly unlikely that there would be practical benefit in facilitating security over coins and banknotes, when money is now typically held in other ways such as in bank accounts. We recommend:

89. For the purposes of the new legislative scheme in relation to pledge, the definition of "corporeal moveable property" should not include money.

(Draft Bill, s 116(1))

Ships

21.7 There is a statutory form of security right for ships, known as a ship mortgage and governed by the Merchant Shipping Act 1995.[7] Ship mortgages require to be registered in the UK Ship Register[8] to have third party effect. The common law also recognises two hypothecs (non-possessory security rights), which are now obsolete in practice, namely the bond of bottomry (over the ship itself) and the bond of respondentia (over the cargo).[9]

21.8 In the Discussion Paper we expressed the view that the project should not deal with shipping law.[10] Our reasons were as follows. First, the existence of the mature system of ship mortgages would cause considerable complexity if a new competing type of security right were to be added, side by side with the existing law. Secondly, the subject-matter of the 1995 Act is reserved to the UK Parliament.[11] We considered that any reform of the law in this area, including for instance the abolition of the obsolete bonds of bottomry and respondentia, would best be done at UK level.

21.9 We suggested that the new security right could be used for vessels in respect of which a ship mortgage is not available and we sought the views of consultees in relation to this. Those who responded to the question all agreed, except for the Faculty of Advocates which said that it had "no particular comment". The WS Society said:

> "We agree with this, but with an important qualification. A ship mortgage can only be granted over a ship registered in part 1 of the Register of Ships (or a fishing boat in part 2). Any ship can be registered in part 1 but smaller ones are not because of the cost and the detailed rules. Therefore we suggest that the new charge should be capable of being granted in relation to a ship which is not registered in parts 1 and 2 of the register."

21.10 We accept this suggestion. It would facilitate the use of small yachts and other minor craft for security purposes, without the need to trouble with registration in the UK Ship Register. It is necessary to provide a little more detail. The UK Ship Register has four parts.[12] Part I is for ships owned by qualifying persons,[13] which are not fishing vessels or small ships. Part II is for fishing vessels, which can be the subject of "simple" or "full

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[7] See G L Gretton, "Ships as a Branch of Property Law" in A R C Simpson, S C Styles, E West and A L M Wilson (eds), *Continuity, Change and Pragmatism in the Law: Essays in Honour of Professor Angelo Forte* (2016) 367 at 394–396.
[8] See https://www.gov.uk/uk-ship-register-for-merchant-ship-and-bareboat-charter-100gt.
[9] See Gloag and Irvine, *Rights in Security* ch 19.
[10] Discussion Paper, para 17.1.
[11] Scotland Act 1998 Sch 5 Part II Head E3.
[12] Merchant Shipping (Registration of Ships) Regulations 1993 (SI 1993/3138).
[13] On the meaning of "qualifying persons", see the 1993 Regulations Part III.

registration".[14] Part III is for small ships.[15] Part IV is for ships registered under the 1995 Act section 7 ("bareboat charter ships").[16] It is not possible for a ship mortgage to be granted over a fishing vessel which is the subject of a simple registration[17] or over a small ship[18] or over a bareboat charter ship.[19] We recommend that:

90. It should not be competent to create a statutory pledge over a ship (or a share of a ship) in respect of which it is competent to register a mortgage in the UK Ship Register.

(Draft Bill, s 47(1)(c))

21.11 This recommendation creates the possibility, albeit a remote one, of a statutory pledge being granted over a yacht, that yacht being subsequently registered in the UK Ship Register and a ship mortgage being granted over it. In this event the usual ranking rule that the security right created earlier ranks first would apply.[20]

Aircraft

21.12 An aircraft mortgage can be created under the Mortgaging of Aircraft Order 1972.[21] Third party effect is dependent on registration in the Register of Aircraft Mortgages.[22] Under the 1972 Order only aircraft registered in the United Kingdom nationality register can be the subject of an aircraft mortgage.[23] We asked consultees whether they agreed that any new security right over corporeal moveable property should not extend to aircraft over which an aircraft mortgage can be granted. All consultees who answered this question agreed, except for the Civil Aviation Authority (CAA) and Faculty of Advocates, both of whom said that they had no comment. We recommend that:

91. It should not be competent to create a statutory pledge over an aircraft in respect of which an aircraft mortgage can be created.

(Draft Bill, s 47(1)(a))

21.13 We do not think it appropriate to undertake a general review of the law of aircraft mortgages, which is UK-wide and reserved to the Westminster Parliament. Nevertheless, the 1972 Order has some specifically Scottish provisions and one of the members of our advisory group, Bruce Wood, drew two difficulties to our attention.

21.14 The first is that there is a style deed for Scottish law but not for English law.[24] Mr Wood advised us that experience has shown that the Scottish style can be awkward to use, and that if no prescribed style is needed in England, none should be needed in

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[14] See the 1993 Regulations reg 3.
[15] A "small ship" is a ship which is less than 24 metres in overall length and which is, or is applying to be registered in Pt III of the UK Ship Register. See 1993 Regulations reg 1(2).
[16] Merchant Shipping Act 1995 s 17. Such ships are registered abroad.
[17] 1993 Regulations reg 3(a).
[18] 1993 Regulations reg 91.
[19] Merchant Shipping Act 1995 s 17(7).
[20] See Chapter 26 below.
[21] SI 1972/1268.
[22] 1972 Order art 14. In correspondence with us in July 2012, the Civil Aviation Authority advised that in the previous three years only eight Scottish aircraft mortgages were registered.
[23] 1972 Order art 3.
[24] 1972 Order art 19 and Sch 2 Part 1 para 2.

Scotland. We asked consultees whether the style should be deleted. Most agreed or had no objection. The Law Society of Scotland and several law firms disagreed, but their responses suggested that they believed that deletion of the style would endanger or indeed end the competence of aircraft mortgages in Scotland. We consider that this concern is misplaced. The style is provided for in Schedule 2 of the 1972 Order, which deals with Scottish aircraft mortgages. The rest of the Schedule would remain. We recommend that:

92. The prescribed style for Scottish aircraft mortgages should be deleted from the Mortgaging of Aircraft Order 1972.

This would require Westminster legislation.[25]

21.15 The second issue identified by Mr Wood was doubt over whether priority notices for aircraft mortgages are competent in Scotland.[26] We asked consultees whether the 1972 Order should be amended to make it clear that this is the case. With one exception, consultees agreed. The exception was the CAA, which is responsible for the Register of Aircraft Mortgages. It was of the view that no amendment is necessary on the basis that article 14 of the 1972 Order, which deals with priority notices, is not restricted to England and Wales. In subsequent correspondence with us, it noted that while Schedule 2 of the 1972 Order amends other articles of the Order in relation to Scotland, it does not amend article 14. Further, in practice the CAA accepts priority notices in respect of Scottish aircraft mortgages. We now accept on general principles of statutory interpretation, as we understand does Mr Wood, that article 14 applies to Scotland. Nevertheless, the 1972 Order could be clearer on the issue. More generally, given that it is now over forty years old, we consider that it would be useful for it to be reviewed. This is true even although its importance is likely to be diminished by the implementation of the Cape Town Convention discussed next.

93. The Mortgaging of Aircraft Order 1972 should be the subject of a UK-wide review.

The Cape Town Convention

21.16 The Cape Town Convention on International Interests in Mobile Equipment covers security interests in "(a) airframes, aircraft engines and helicopters; (b) railway rolling stock; and (c) space assets."[27] The Convention itself is a framework convention, which works with its protocols. Three protocols exist, for the three separate classes of asset.[28] Work has commenced on a fourth protocol in relation to agricultural, construction and mining equipment (the "MAC Protocol"). The reason for the Convention is that the equipment it covers very commonly moves between different countries and therefore there is much to be

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[25] More precisely an Order in Council under the Civil Aviation Act 1982 s 102 and Sch 13 Part II subject to the negative resolution procedure).

[26] W A Wilson, *Scottish Law of Debt* (2nd edn, 1991) para 7.6 states that they are.

[27] UNIDROIT Cape Town Convention art 2(3). See http://www.unidroit.org/instruments/security-interests/cape-town-convention.

[28] The First Protocol is for airframes, aircraft engines and helicopters.
See http://www.unidroit.org/english/conventions/mobile-equipment/aircraftprotocol.pdf.
The Second Protocol is for railway rolling stock.
See http://www.unidroit.org/instruments/security-interests/rail-protocol.
The Third Protocol is for space assets.
See http://www.unidroit.org/instruments/security-interests/space-protocol.

said for an internationally recognised form of security interest, known as an "international interest".

21.17 The Convention is heavily influenced by UCC–9.[29] It is asset-specific, so that (in contrast to UCC–9 and the PPSAs) the possibility of security over generic future assets does not exist.[30] The international registry which it created for aircraft is based in Dublin.[31] When the Discussion Paper was published in 2011, the position was that the UK had signed the Convention but not ratified it.

21.18 Article 52 of the Convention enables contracting States to ratify it for the whole State or part of it. We asked consultees whether they considered that the UK Government should accede to the Convention (either for the whole UK or for Scotland only). Consultees were generally supportive of accession on a UK-wide basis or had no opinion. No consultee supported Scotland-only accession.

21.19 Prior to the publication of the Discussion Paper, the then Department for Business Innovation and Skills (DBIS)[32] had issued a call for evidence in relation to UK-wide ratification of the First Protocol on airframes, aircraft engines and helicopters (known collectively as "aircraft objects"). In December 2013 it announced that it had decided to proceed with ratification.[33] In June 2014 DBIS published a consultation document on options for implementation.[34] This led to the promulgation of the International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015.[35] On 27 July 2015 the UK instruments of ratification were deposited with UNIDROIT and the Convention came into force in the UK on 1 November 2015.[36] As we have seen, the consultees to our Discussion Paper mainly favoured UK-wide accession and we therefore welcome this. None of our consultees made specific comments on accession to the Second and Third Protocols (respectively railway rolling stock and space assets).

21.20 In cases where it is competent to create an international interest in airframes, aircraft engines and helicopters under the 2015 Regulations, we do not think that the statutory pledge should be used. We recommend that:

94. It should not be competent to create a statutory pledge over an aircraft object in respect of which an international security interest can be created under the International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015.

(Draft Bill, s 47(1)(b))

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[29] The standard text is R M Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment* (2nd edn, 2008). See also Discussion Paper, Appendix A.

[30] But the Protocol to the Convention on International Interests in Mobile Equipment on Matters specific to Railway Rolling Stock (2007) says that the description of railway rolling stock can be "a statement that the agreement covers all present and future railway rolling stock" (art V(1)).

[31] See https://www.internationalregistry.aero/irWeb/Controller.jpf.

[32] Since July 2016, the Department for Business, Energy and Industrial Strategy.

[33] See DBIS, Ratification of the Convention on International Interests in Mobile Equipment and Protocol thereto on Matters Specific to Aircraft Equipment (June 2014) p 3, available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/320482/bis-14-452-ratification-of-convention-on-international-interests-in-mobile-equipment-aircraft-equipment-protocol-consultation.pdf.

[34] See the previous footnote.

[35] SI 2015/912.

[36] See generally M Bisset, "Ratification of the Cape Town Convention by the United Kingdom" (2016) 49 Air & Space Law 49.

Motor vehicles

21.21 In the Discussion Paper we noted that in some countries the registration of motor vehicles is a system of title registration and that security can happen as part of that register.[37] In the UK the registration system operated by the Driver and Vehicle Licensing Agency (DVLA) is administrative. It is separate from private law. Thus, for example, registration with the DVLA is not necessary for the transfer of ownership of a vehicle.[38]

21.22 The statutory pledge could be granted over motor vehicles by registration in the Register of Statutory Pledges. If the experience in PPSA systems is repeated then motor vehicles are likely to be frequently the subject of the new statutory pledge, not least in relation to private individuals. The statutory pledge would offer an alternative to arrangements such as hire-purchase and conditional sale, and allow the debtor to have ownership of the vehicle rather than this being held by a finance company.

21.23 As we have mentioned elsewhere,[39] arrangements such as hire-purchase are no good where the debtor already has ownership but wishes to use the vehicle as collateral. Here the introduction of the statutory pledge has the potential to make a significant difference to the availability of vehicles for security purposes.

21.24 Later in this Report we recommend similar protections for good faith private purchasers of motor vehicles as currently exist where such a vehicle is the subject of a hire-purchase agreement.[40]

21.25 A final issue about motor vehicles is that their unique vehicle identification number (VIN) enables them to be traced, where the owner has transferred the vehicle to a third party without the secured creditor's permission. Later in this Report we recommend that it should be possible for VINs to be registered in the RSP and be capable of being searched against.[41] We recommend also that the protection for good faith acquirers where there is a supervening inaccuracy in relation to the provider's details should not apply where property has a unique number (being a class of property prescribed in RSP Rules) and that number is in the entry.[42] We have VINs in mind here. Thus imagine that Alan grants a statutory pledge to the Ballindalloch Bank over his car and the bank registers the VIN in the entry in the RSP. Alan then sells the car to C Ltd without the bank's permission. C Ltd then sells to D Ltd. D Ltd would be unable to find the statutory pledge by a search against C Ltd because the statutory pledge is registered against Alan and it should in principle be protected if it is in good faith. But here the statutory pledge could be found by a search against the VIN.

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[37] Discussion Paper, para 17.4.
[38] See Gretton and Steven, *Property, Trusts and Succession* para 5.20.
[39] See para 17.21 above.
[40] See paras 24.34–24.43 below.
[41] See paras 30.7–30.8 and 34.6 below.
[42] See Chapter 32 below.

Chapter 22 Incorporeal moveable property

Introduction

22.1 This chapter considers security over incorporeal moveable property. In the Discussion Paper we divided this type of property into (a) claims, monetary and otherwise and (b) other types of incorporeal moveable property.[1] Within (b) we listed intellectual property, company securities[2] (shares and bonds), public sector bonds, intermediated securities and negotiable instruments.[3]

22.2 For incorporeal moveable property there simply exists no "true" (or "proper")[4] security right. Under the current law only functional security can be achieved, by transferring the asset to the creditor by means of assignation. Thus taking security over financial instruments or intellectual property requires transfer of the asset to the creditor. As discussed elsewhere, the result is to give the creditor a more extensive right than is needed, resulting in problems in practice.[5] For example, security can only be taken once. It is thus not possible to have multiple securities over the same asset.

22.3 We asked consultees whether the concept of a "proper" security over incorporeal moveable property should be introduced into Scots law. All the consultees who answered this question agreed, with the exception of Jim McLean who had in mind an alternative scheme based on assignation. Two law firm consultees argued that such a reform would be "useful and desirable".[6] Alisdair MacPherson commended it as "positive", adding that there are "obvious commercial advantages offered by the fact that more than one security could be granted over the asset and the ability of the debtor to transfer the right to another party subject to the security." We agree therefore that the statutory pledge should be available in respect of incorporeal moveable property.

22.4 The question then arises as to the types of that property which could be the subject of the new security right. Prior to the publication of the Discussion Paper, our advisory group took the view that it should be available for all types of incorporeal moveable property. This indeed is the general position under UCC–9, the PPSAs, the DCFR and the UNCITRAL Model Law.[7] This was also supported by many of the consultees who responded to the Discussion Paper. Nevertheless, for the reasons which we set out below and after much consideration, we recommend that the statutory pledge should, at least initially, only be available in respect of incorporeal moveable property for certain asset classes.

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[1] Discussion Paper para 19.1. In comparison in Chapter 7 of the Discussion Paper in relation to the current law, we distinguished between (a) personal rights as collateral and (b) intellectual property.
[2] The word "securities" of course here has a different meaning from security rights.
[3] For an overview of the special types of incorporeal moveable property, see Discussion Paper, Chapter 7.
[4] In other words a subordinate right. See para 17.2 above.
[5] See paras 17.12–17.16 above.
[6] Dundas & Wilson, and McGrigors.
[7] See, for example, Drobnig and Böger, *Proprietary Security in Movable Assets* 214.

Claims

General

22.5 In the Discussion Paper we asked whether the new security right should apply to all types of claim,[8] and not just some types, such as receivables. Consultees generally agreed. ABFA and the WS Society said: "It seems generally undesirable to distinguish the types of security right which can apply to anything falling within the brocard of incorporeal moveable property unless there is good reason to do so – otherwise why have the brocard." Scott Wortley, however, noted that "whether such securities should be created over all claims is tricky as it is dependent in part on the reforms to the general law of assignations."

22.6 We consider now that there are two major difficulties in permitting a statutory pledge to be created over claims.

Difficulty (a): inter-relationship with assignation in security of claims

22.7 The first difficulty is that alluded to by Mr Wortley, namely how a statutory pledge over claims would interface with an assignation in security over claims. We noted in the Discussion Paper that if a new form of security right over claims were to be introduced an assignation in security would arguably then no longer be necessary.[9] Thus when the standard security was introduced it ceased to be competent to transfer heritable property for the purpose of security.[10] Nevertheless, a counter-argument is that distinguishing outright assignation from assignation for the purpose of security is extremely difficult.[11]

22.8 The approach under UCC–9, the PPSAs, the DCFR and the UNCITRAL Model Law is not to prohibit assignations in security but rather to recharacterise them as security rights.[12] This was also the position under the new Belgian Pledge Act of 11 July 2013, as originally passed, for the assignation in security of receivables,[13] although the legislation was amended in 2016 to remove security over receivables from the new scheme.[14] In contrast, the Dutch Civil Code debars transfers for security purposes, but the impact of the relevant provision has been restricted by case law.[15] Prohibiting assignation in security, and recharacterising assignation in security as a proper security right are similar in substantive effect. The former says "assignation in security is void" and the other says "assignation in security is valid, but takes effect not as an assignation but as a proper security right". Under

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[8] That is to say claims which are moveable. Our recommendations on assignation of claims extend to certain heritable claims. See paras 4.12–4.16 above.
[9] Discussion Paper, para 18.33.
[10] Conveyancing and Feudal Reform (Scotland) Act 1970 s 9.
[11] Although the same may in principle be said of transfers of other types of property. Note the Sale of Goods Act 1979 s 62(4).
[12] On recharacterisation, see para 18.8 above.
[13] Belgian Pledge Act of 11 July 2013 art 73 (which provided for art 62 of the new Book III title XVII of the Civil Code).
[14] See http://www.cms-lawnow.com/ealerts/2016/12/belgian-reform-of-security-interests-over-movable-assets-postponed-further-and-slightly-amended.
[15] Dutch Civil Code art 3:84(3): "*Een rechtshandeling die ten doel heeft een goed over te dragen tot zekerheid … is geen geldige titel van overdracht van dat goed*." ("A juridical act that is intended to transfer property for the purpose of security … does not constitute a valid title for the transfer of that property.") See in particular *Keereweer v Sogelease BV* (HR 19-05-1995, NJ 1996, 119), discussed in S van Erp and B Akkermans (eds), *Cases, Materials and Text on Property Law* (2012) 513–515. The rule also does not apply to financial collateral arrangements. See Dutch Civil Code art 7:55. See also R G Anderson and J W A Biemans, "Reform of Assignation in Security: Lessons from the Netherlands" (2012) 16 EdinLR 24 at 39–41.

both approaches the effective result is no assignations in security, but only proper security rights.

22.9 Where the Financial Collateral Arrangements (No. 2) Regulations 2003 (FCARs)[16] apply an assignation in security must be given effect according to its terms. Therefore prohibiting or recharacterising such an assignation is not possible.[17]

22.10 We asked consultees whether, if a new type of moveable security right were introduced, assignation in security should cease to be competent. A clear majority of consultees including ABFA, the Judges of the Court of Session, the Law Society of Scotland and several law firm consultees favoured retention of assignation in security. The Law Society observed that "since assignation in security must remain competent for certain cases (financial collateral) it makes more sense for the assignation in security to continue to be available across the board." David Cabrelli, Chris Dun and the Faculty of Advocates, however, disagreed. Professor Eric Dirix favoured recharacterisation.

22.11 It seems to us that recommending a prohibition on assignation in security even where this would be permissible because the FCARs are not applicable, would attract significant opposition. It would no doubt require existing practices to be rethought, which would increase transaction costs. But if assignation in security is to be (i) retained in respect of claims and (ii) made far more commercially viable by being completed by registration in the Register of Assignations rather than intimation, it may be questioned how strong the case is for allowing the statutory pledge in respect of claims.

Difficulty (b): control

22.12 The second major difficulty in relation to the statutory pledge where claims are the encumbered property concerns the fact that this would be a fixed security. It would in effect be the Scottish counterpart of the English fixed charge. If the provider were a company or LLP, it would be subject to the same legislation in the event of insolvency, that is to say the Insolvency Act 1986. For the statutory pledge to be treated as a fixed security in relation to claims such as receivables would therefore seem to necessitate trying to imitate the English law rules on "control" of the *proceeds* of the claims. These rules, which we discuss elsewhere,[18] are fiendishly difficult and unclear. In the broadest terms what seems to be needed is for the proceeds to be paid into a blocked bank account from which the secured creditor must give specific permission for any money to be released.

22.13 This issue previously attracted attention in 1994 when the Murray Report seemingly proposed a fixed security over receivables but without requiring control over proceeds.[19] This resulted in a careful and detailed submission from this Commission, principally authored by Professor Niall Whitty. It stated:

> "We suspect that a fixed moveable security over future book debts would be very popular with both secured creditors and borrower incumbrancers in Scotland. The secured creditors would be attracted inter alia by the priority over preferential

[16] SI 2003/3226. See Chapter 14 above.
[17] See para 14.19 above.
[18] See paras 20.27–20.33 above and para 22.16 below.
[19] The draft Floating Charges and Moveables Securities (Scotland) Bill appended to the Murray Report in clause 9 provides that the "moveable security" can be granted over receivables, but there are no provisions on control of proceeds.

creditors. The borrowers would be attracted by the freedom of management over the proceeds of the receivables. ...

We find it very difficult however to support the notion of a fixed security over receivables which gives the debtor freedom of disposal of the proceeds. …

In Scots law a fixed security may be broadly defined as a real right in the property of another which secures the performance of an obligation. In the case of an assignation in security of a future incorporeal debt to become due by an identifiable debtor, intimation creates the assignee's real right under Scots law and subsequent attempts by the assignor at collection will be refused by the debtor unless the assignee consents. The assignation plus intimation creates a genuine real right which is in stark contrast to the purported or sham real right [proposed]."[20]

22.14 The comments in the final paragraph are rather echoed by Lord Hope of Craighead in the subsequent landmark English decision of *National Westminster Bank plc v Spectrum Plus Ltd*[21] where he states:

> "[S]ubjecting book debts to a security which will be effective as a fixed charge in Scots law . . . is far less convenient [than a floating charge] in practice. This is because the law of Scotland still insists that a fixed charge can be created only by delivery of the property which is to be subjected to it in the hands of the creditor or by the equivalent of delivery. The only way in which this can be done in the case of book debts is by obtaining an assignation in security of the right to receive payment of the debt, which is then intimated to the party who is liable to pay the debt to the company."

22.15 We discussed the arguments made by Professor Whitty in some detail with our advisory group. We also explored the issue of control with insolvency experts with whom we held a meeting. Some were supportive of the position that control over proceeds is necessary to achieve a fixed security over claims. Others dissented. A cautious approach therefore is that control of proceeds is required.

22.16 In England and Wales, the rules distinguishing fixed and floating charges, and on the level of control of proceeds necessary to achieve a fixed charge, rest in equity.[22] They are not statutory. As we recounted above,[23] the case law on receivables and their proceeds has ebbed and flowed from *Siebe Gorman & Co v Barclays Bank*[24] to *Spectrum Plus* (above) and it is difficult to know exactly what the law is. There is widespread agreement that this is one of the most unsatisfactory areas of English commercial law and in 2014 the Financial Law Committee of the City of London Law Society published a Discussion Paper on the matter.[25]

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[20] Comments by Scottish Law Commission on Consultation Paper by Department of Trade and Industry on Security over Moveable Property in Scotland (November 1994), 16 March 1995 paras 3.45–3.47.
[21] [2005] UKHL 41.
[22] See generally Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* paras 6.106-6.139 and Calnan, *Taking Security* paras 4.79–4.125.
[23] See paras 20.31–20.33 above.
[24] [1979] 2 Lloyd's Rep 142.
[25] The Discussion Paper is available at http://www.citysolicitors.org.uk/attachments/article/121/20140219%20Secured%20Transactions%20Reform%20Discussion%20Paper%202%20Fixed%20and%20floating%20charges%20v2.pdf. It sets out three options: (1) to clarify the distinction between fixed and floating charges; (2) to identify particular assets out of which a levy in favour of certain preferential claims should be paid; and (3) to pay the levy as a small percentage of all charged assets subject to a cap.

In 2017 the Secured Transactions Law Reform Project also published a Discussion Paper.[26] English law may well be reformed in the coming years. Therefore attempting to put such unsatisfactory and difficult rules into our draft Bill is undesirable.

22.17 Nevertheless, without control provisions a statutory pledge over claims could distort the balance between secured and unsecured creditors in corporate insolvencies. As we have noted elsewhere,[27] insolvency law is in principle outwith the scope of this project. We cannot, however, ignore the fact that the two areas are closely related and that facilitating more security potentially has an adverse effect on unsecured creditors. Several consultees, notably the Faculty of Advocates and Scott Wortley, commented on this, as did the insolvency specialists with whom we met.

Conclusion

22.18 It therefore seems to us, particularly given the availability of assignation in security in respect of claims, that permitting the statutory pledge to be granted over claims, especially without control provisions, cannot presently be justified. We say this with some hesitation given that it is one of the key objectives of the UNCITRAL Legislative Guide on Secured Transactions that security should be facilitated over all types of asset,[28] but we have concluded that local circumstances require a deviation from this. The position may of course change in the future not least if there are developments in England and Wales, and corporate insolvency law is reformed, but for the moment we are of the view that claims should be outwith the scope of the statutory pledge.[29]

Assignations in security and control of proceeds

22.19 There remains another difficult question. Where claims are assigned in security, should it be a requirement that the assignee has control over the proceeds? Thus, Professor Whitty and Lord Hope in the statements quoted above say that the "control" requirement in English law is replicated in Scottish law by the requirement for intimation to the (account) debtor. Earlier in this Report we recommend that registration in the new Register of Assignations should be an alternative to intimation.[30] This is especially to facilitate the assignation of future claims. Where the assignation is in security it may, however, be argued that registration alone should be insufficient and that there should also require to be control of proceeds.

22.20 We have also found this matter highly challenging, but ultimately we have concluded against including provisions in our draft Bill on control of proceeds for assignations in security of claims. Our reasons are as follows. First, an assignation is not a proper security right.[31] It is a transfer.[32] To be more exact, it is a transfer in security. In England and Wales

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[26] The Discussion Paper is available at: https://stlrp.files.wordpress.com/2017/01/paterson-fixed-and-floating-charges.pdf. The author is Professor Sarah Paterson. It canvases possibilities for reform.
[27] See para 1.26 above. See also paras 18.69–18.71 above.
[28] UNCITRAL Legislative Guide on Secured Transactions at 21 (key objective (e)).
[29] Below at paras 22.30–22.34 we set out an exception for claims which fall within the definition of "financial instrument".
[30] See Chapter 5 above.
[31] Compare with the position in South Africa where an assignation in security of a claim (cession *in securitatem debiti*) can be characterised as a pledge. See P Nienaber and G Gretton, "Assignation/Cession" in R Zimmermann, D Visser and K Reid (eds), *Mixed Legal Systems in Comparative Perspective: Property and Obligations in Scotland and South Africa* (2004) 787 at 814–818.
[32] For a detailed analysis, see A D J MacPherson, *The Attachment of the Floating Charge in Scots Law* (PhD Thesis, University of Edinburgh, 2017) 238–264.

equitable assignments for security purposes are commonly treated synonymously with fixed or floating charges and characterised as such.[33] The idea of an assignation being characterised as a floating charge is at odds with property law in Scotland where floating charges are not recognised under our common law.[34]

22.21 Secondly, leaving aside their inherent complexity in English law, proceeds rules would be very difficult to operate in the context of an assignation as a transfer. Imagine that an assignation in security requires proceeds to be held in a blocked bank account. X Ltd assigns certain future invoices to Y Ltd. X Ltd arranges for the account debtors to make payment into a blocked account. The account is subsequently "unblocked". What is to be the effect? The notion that the assignation is thereby invalidated and the right to the claims and therefore the proceeds is automatically revested in X Ltd is unattractive. And if the account is blocked again? Does that revalidate the assignation? There would have to be recharacterisation, which again would run counter to our property law and the views of our consultees.

22.22 Thirdly, assignation in security is an existing part of the law in Scotland. Our recommendations are to reform how it may be completed. This may be contrasted with the statutory pledge which would be an innovation.

22.23 Fourthly, at a practical level, even without a statutory requirement the assignee will want to assert a measure of control over the proceeds, otherwise it will be unprotected in the event of the assignor's insolvency. Thus the assignee may insist that the proceeds are held in trust for it and paid over to it at regular intervals. An assignation in security of claims is of little value if the assignor is able to dissipate the proceeds. Another form of protection is for the assignee to intimate and require payment from the account debtor. When this is done in South Africa the sums recovered are applied in satisfaction of the secured debt and any surplus held to the order of the assignor.[35]

22.24 Fifthly, if it is considered necessary for the purposes of corporate insolvency law to recharacterise an assignation in security as a floating charge where there is a lack of control of proceeds, this could be taken forward by reform of the corporate insolvency legislation. As we have mentioned above, there is already pressure in England and Wales for the different treatment of fixed and floating charges in an insolvency to be reviewed.

Financial instruments

General

22.25 In the Discussion Paper we saw particular advantages resulting from the availability of the new security right for financial instruments, such as shares in a company.[36] This is because under the current law security can only be achieved by transfer, even although

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[33] See G Tolhurst, *The Assignment of Contractual Rights* (2nd edn, 2016) para 3.17. See also Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* paras 4-13–4.37.

[34] *Carse v Coppen* 1951 SC 233 at 239 per Lord President Cooper. See also R Anderson, "Security over bank accounts" 2010 Law and Financial Markets Review 593 at 599 in relation to assignation of claims in respect of bank accounts (discussed below at para 22.57): "Because a Scottish pledge over account operates by way of title transfer, any concession of a right to the account holder to operate the account does not destroy the security. In other words, *Spectrum Plus* has no application to pledges of account."

[35] Nienaber and Gretton, "Assignation/Cession" at 817.

[36] Discussion Paper, paras 19.4–19.5.

such a transaction is misleadingly named a "pledge of shares" or "shares pledge".[37] Thus in the Supreme Court case of *Farstad Supply A/S v Enviroco Ltd*[38] a bank took a transfer of company shares in security. This resulted in unwelcome consequences, in that the company whose shares were being used as collateral thereby ceased, for the time being at least, to be the subsidiary of the debtor company. In general terms the drawbacks of security by transfer which we outlined earlier apply.[39] The secured creditor acquires greater rights than it actually needs. Thus as registered holder of the instrument it is entitled to dividends or interest and, in the case of shares, to vote at shareholder meetings.

22.26 Another issue in relation to Scottish shares pledges has arisen since 1 April 2016 because of the new requirement for companies and LLPs to maintain a "Person of Significant Control (PSC) Register".[40] Registration is required of any individual or "relevant registerable legal entity"[41] which exercises specified methods of significant control of the company or LLP, for example, holding (directly or indirectly) 25% or more of the shares in the company.[42] Various criminal offences apply where there is failure to comply with the requirements.[43] The new legislation has a carve-out for security in respect of shares:

> "Rights attached to shares held by way of security provided by a person are to be treated for the purposes of this Schedule as held by that person—
>
> (a) where apart from the right to exercise them for the purpose of preserving the value of the security, or of realising it, the rights are exercisable only in accordance with that person's instructions, and
>
> (b) where the shares are held in connection with the granting of loans as part of normal business activities and apart from the right to exercise them for the purpose of preserving the value of the security, or of realising it, the rights are exercisable only in that person's interests."[44]

22.27 A consensus has now been reached by major law firms that this carve-out does apply to Scottish share pledges although they involve the transfer of the shares rather than taking a security right in the shares. But this is another example of a complexity arising from the lack of a "proper" security over shares.

22.28 Under English law it is possible to use an equitable security right (charge), which leaves the provider company as the registered holder of the instrument.[45] This means that the various difficulties caused by transfer can be avoided.

22.29 There was strong support from our advisory group for the statutory pledge to be available in respect of financial instruments. The current Scottish law requiring transfer was regarded as comparing very badly with the position of England and Wales. In addition,

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[37] See eg *Braithwaite v Bank of Scotland* 1999 SLT 25. See Steven, *Pledge and Lien* para 5-05.
[38] [2011] UKSC 16.
[39] See paras 17.12–17.16 above.
[40] Companies Act 2006 Part 21A and Sch 1A, inserted by the Small Business, Enterprise and Employment Act 2015 s 81 and Sch 3. We are grateful to Andrew Kinnes for drawing this to our attention and also to Gillian Frew for her assistance.
[41] Companies Act 2006 s 790C(8).
[42] Companies Act 2006 Sch 1A Part 1 para 2.
[43] Companies Act 2006 ss 790F, 790Q and 790R.
[44] Companies Act 2006 Sch 1A Part 3 para 23.
[45] See generally Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* paras 3.19–3.24.

Michael Royden, a consultee to the Discussion Paper, while noting that the availability of the new security would create additional issues in corporate transactions, thought that the lack of a formal pledge[46] over shares in Scots law was "a disadvantage" and that it would be "useful" to resolve the issue.

Definition

22.30 Clearly "financial instrument" requires definition. We have concluded in discussion with our advisory group that it would make sense to draw on the definition in the FCARs. This is because this definition, despite some uncertainties,[47] already has application in relation to creating security over financial instruments. Mapping on to it is therefore a simpler approach than trying to provide a bespoke definition which would nevertheless have to interact with it. We discuss the FCARs and their requirements in Chapter 14 above and Chapter 37 below. The definition of "financial instruments" is:

> "(a) shares in companies and other securities equivalent to shares in companies;
>
> (b) bonds and other forms of instruments giving rise to or acknowledging indebtedness if these are tradeable on the capital market; and
>
> (c) any other securities which are normally dealt in and which give the right to acquire any such shares, bonds, instruments or other securities by subscription, purchase or exchange or which give rise to cash settlement (excluding instruments of payment);
>
> and includes units of a collective investment scheme within the meaning of the Financial Services and Markets Act 2000, eligible debt securities within the meaning of the Uncertificated Securities Regulations 2001, money market instruments, claims relating to or in respect of any of the financial instruments included in this definition and any rights, privileges or benefits attached to or arising from any such financial instruments".[48]

22.31 This definition effectively comes in four parts: (a), (b), (c) and express inclusions. Part (a) clearly includes shares in both limited and public limited companies. The expression "securities equivalent to shares in companies is less straightforward, but may include membership certificates and depositary receipts.[49] Part (b) includes public sector bonds, such as those issued by HM Government and local authorities. For a security to fall within part (c) it must be shown that there is normally a market for it, even though they do not have to be traded on an exchange and there could be times in which no market exists.[50]

Intermediated securities

22.32 In relation to the express inclusions, it is the final "sweep up" wording that is particularly important. It refers to "claims relating to or in respect of" financial instruments and thus includes intermediated securities. An intermediated security is where, for

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[46] While one talks of a pledge of shares under the current law this is actually a transfer. See Steven, *Pledge and Lien* para 5-05.
[47] See further Yeowart and Parsons, *The Law of Financial Collateral* paras 3.26–3.61. Professor Gretton has described it as "vague". See G L Gretton, "Financial Collateral and the Fundamentals of Secured Transactions" (2006) 10 Edin LR 209 at 211.
[48] Financial Collateral Arrangements (No. 2) Regulations 2003 (SI 2003/3226) reg 3(1).
[49] Yeowart and Parsons, *The Law of Financial Collateral* paras 3.35–3.36.
[50] Yeowart and Parsons, *The Law of Financial Collateral* paras 3.52.

convenience, shares or bonds are not held directly but indirectly. For example, a company issues shares and an investor wishes to buy some of these. The investor could hold the shares directly, but alternatively the shares can be held by an intermediary, such as a member of the CREST system,[51] on behalf of the investor. The intermediary receives the dividends and passes these to the investor. If the investor decides to sell the shares, the intermediary will sell them and give the proceeds to the investor.

22.33 The investment therefore consists of a claim (personal right) against the intermediary.[52] That claim could be assigned in security under the current law. Earlier in this chapter we concluded that claims should in principle be excluded from the scope of the statutory pledge at least initially. We consider that an exception should be made for claims falling within the definition of "financial instrument" on which we are drawing from the FCARs in the interests of applying that definition consistently. Our advisory group supported the availability of the statutory pledge for intermediated securities because multiple statutory pledges are possible. In contrast, an assignation in security, as a transfer, can only be done once.

22.34 We recommend:

95. It should be possible to create a statutory pledge over financial instruments within the meaning of regulation 3(1) of the Financial Collateral Arrangements (No. 2) Regulations 2003.

(Draft Bill, ss 47(2)(c) and 116(1))

Intellectual property

General

22.35 Intellectual property (IP) has become an important type of incorporeal moveable property for the purposes of granting security because of the increasing value of this type of asset.[53] It is therefore detrimental to our legal system's reputation that, in the words of an article published on the law firm Brodies' website, Scottish law here is "stuck in the 19th century".[54] In an important independent report commissioned by the Intellectual Property Office and published in 2013 it was concluded that more needed to be done to encourage SMEs to use their IP to access finance.[55] Facilitating the granting of security rights is an

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[51] The system for the holding of dematerialised securities. See the Uncertificated Securities Regulations 2001 (SI 2001/3755). See generally Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 3.23.

[52] The position in English law and some other systems is more complicated. The position of the investor is regarded as a bundle of rights, some of these being contractual rights against the intermediary and others being "proprietary rights" in the underlying investments. See J Benjamin, *Interests in Securities* (2000) and Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* paras 3.25–3.26.

[53] See eg I Davies, "Technology-based small firms and the commodification of intellectual property rights" in De Lacy (ed), *The Reform of UK Personal Property Security Law* 308 and M Abraham, "Tapping the intangible: security interests and intellectual property" 2013 Insolvency Intelligence 113. In 2009 the World Intellectual Property Office estimated that global commerce in IP was worth US $300 billion worldwide annually. See World Intellectual Property Office, *Information Paper on Intellectual Property Financing* (2009) 4, available at http://www.wipo.int/edocs/mdocs/copyright/en/wipo_ip_fin_ge_09/wipo_ip_fin_ge_09_7-main1.pdf.

[54] See http://www.brodies.com/blog/security-over-ip-scots-law-stuck-in-the-19th-century/.

[55] Intellectual Property Office, *Banking on IP? The role of intellectual property and intangible assets in facilitating business finance: Final Report* (2013) available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/312008/ipresearch-bankingip.pdf. The report was written by Martin Brassell and Kelvin King.

important part of this. Also in 2013 the Department for Business, Innovation and Skills[56] noted that: "Smaller and newer firms, which often have less security to use as collateral, or firms with intangible assets such as intellectual property, find it harder to raise finance."[57]

22.36 The principal difficulty in current Scottish law highlighted earlier in this Report is that the only way in which security can be achieved is by transfer (assignation).[58] This means that complex contractual arrangements have to be entered into to license the IP back to the party which is providing it as collateral. Further, an assignation, as a transfer, can only be granted in favour of one secured creditor. It is impossible to grant several effective assignations of the same IP.

22.37 In an exchange with us following consultation, Scottish Enterprise expressed particular support for the new security being available in respect of IP:

> "Existing methods of taking security over IP (assignation in security with a licence back to the debtor) are fairly restrictive and the cost and management implications to the creditor of maintaining the IP registrations (patents, trademarks etc,) and ensuring that IP created by the debtor after the date of grant of the security is captured under the security can cause potential lenders to avoid advancing lending against IP assets. If the new security would allow the IP registrations to remain with the debtor whilst the creditor can obtain a registerable security interest in the IP then this may be a valuable addition to the suite of securities available to lenders in Scotland."

22.38 But, in a very detailed submission, Dr Andreas Rahmatian set out what he saw as the potential difficulties with the proposed new security right being available for IP.[59] His starting point was the fact that IP law is reserved under the Scotland Act 1998.[60] It is therefore not possible for an Act of the Scottish Parliament on security rights to amend existing UK legislation to the extent that IP is reserved. Dr Rahmatian contended that the inter-relationship between the new security right and the existing method of achieving security, namely by assignation (or assignment), would be difficult. Thus while the new security right could be discovered by a search in the Register of Statutory Pledges (RSP), an assignation would not be. The RSP would therefore not be definitive. He also drew attention to international private law issues. He pointed out the complications that would result where Scottish IP subject to the new security right was assigned to someone in another jurisdiction such as England and the assignee then granted a further security right over it there.

22.39 We do not doubt that there are problems here. In particular there is a need to clarify international private law in relation to IP, not least between Scotland and England.[61] As regards the issue of IP being reserved, our policy is that our draft Bill should work within the framework of the existing UK statutory regimes on IP, and we say more on this shortly.[62] Our conclusion, however, is that the difficulties that exist do not justify precluding the

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[56] Since July 2016 the Department for Business, Energy and Industrial Strategy.

[57] Department for Business, Innovation and Skills, *Building the Business Bank: Strategy Update March 2013* (2013) 10 available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/203148/bis-13-734-building-the-business-bank-strategy-march-2013.pdf.

[58] See paras 17.12–17.16 above. See also J Macfarlane and S Macpherson, "Securities over Intellectual Property in Scotland" 1993 The In-House Lawyer 18.

[59] We are also grateful to Dr Rahmatian and Mr Jim McLean for attending a special advisory group meeting on this issue in March 2014 and providing us with their expertise there.

[60] Scotland Act 1998 Sch 5 Part II Head C4. But some parts of the law of plant varieties are devolved.

[61] See Chapter 39 below.

[62] See also para 1.47 above.

statutory pledge being made available in respect of IP. We consider that the benefit of having a security right which does not necessitate transfer is a substantial one. It would be an important innovation at a time when IP is increasingly valuable as potential collateral.

22.40 There would also be benefit in facilitating security over applications for IP and for IP licences where possible.[63] Thus the Patents Act 1977 makes clear that any patent, or application for a patent, or right in or under a patent, is incorporeal property which may be the subject of a security right.[64]

22.41 As regards licences of IP some may not be suitable for being the subject of the statutory pledge because they are provided to be non-transferable.[65] Moral rights would also be excluded for the same reason.[66]

22.42 Allowing the statutory pledge over IP when an assignation in security continues to be available, while bringing Scottish law into line with the other parts of the UK, does of course create a level of duplication. There may be much to be said for more radical reform.[67] But for pragmatic reasons this is beyond the scope of this Report. In particular, provisions restricting the assignation of IP for security purposes would require UK legislation and are thus beyond the legislative competence of the Scottish Parliament.

22.43 We therefore recommend:

96. It should be possible to create a statutory pledge over:

(a) intellectual property, and

(b) applications for, or licences over, intellectual property.

(Draft Bill, s 47(2)(a) & (b))

Registration

22.44 The result of our recommendations would be to introduce an important new option for security over IP. Creditors would thus have a choice. They could achieve security by transfer as under the existing law. Alternatively, the statutory pledge could be used.

22.45 IP can be broadly divided into two categories: unregistered (such as copyright) and registered (such as patents). For unregistered IP, the choice would work in the following way. The parties could do what is done at present ie assign the copyright, by way of security, with the assignation not being registered (except, in cases where the provider is a company etc, under the company charges registration scheme). Or they could use the new

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[63] The UK Intellectual Property Office "Fast Facts 2017" publication states that global trade in IP licences in 2014 was worth more than £220 billion (1.6% of global trade) and rising. See https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/581279/Fast-Facts-2017.pdf.

[64] Patents Act 1977 s 31(1) and (3). The provisions also apply to applications for a European patent (UK) by virtue of s 78 of that Act See also the Registered Designs Act 1949 s 15B(6) and the Trade Marks Act 1994 ss 24(5) and 27.

[65] See paras 19.63–19.65 above. For provisions on licences, see eg the Patents Act 1977 s 31(4), the Trade Marks Act 1994 s 28(1), the Registered Designs Act 1949 s 15B(7) and the Copyright, Designs and Patents Act 1988 s 90(4).

[66] Copyright, Designs and Patents Act 1988 s 205L.

[67] See S Thomas, "Security Interests in Intellectual Property" 2017 Legal Studies 214.

statutory pledge, which would leave title to the copyright being held by the provider. The statutory pledge would be registered in the RSP.

22.46 For registered IP, the same choice would exist, but there would be a complicating factor. In the Discussion Paper[68] we concluded that the IP legislation leaves the question of security rights to general law, thus leaving Scots law able to develop an alternative to assignation in security. But we also concluded that in some cases such a security right would, because of the provisions of the relevant legislation, be precarious unless registered in the appropriate IP register. In other words, it would be vulnerable to third parties acquiring rights over the property which would trump the unregistered security right. Thus suppose that X held a patent and wished to grant a statutory pledge over it to Y. If the rule is to be that the statutory pledge must be registered in the RSP and that is indeed the rule which we now recommend in Chapter 23 below,[69] then Y might wish to ensure that the security right would not be precarious by registering it also in the Patents Register. That would be double registration. This could be criticised as being inconvenient and adding expense.

22.47 One possibility would be to amend the IP legislation so as to allow registration in the RSP to suffice. But this would require UK legislation. Another possibility would be to provide that registration in the relevant intellectual property register would suffice. So the statutory pledge by X to Y could be registered in the Patents Register, and that would be all that would be needed. Attractive though that solution would seem, it would not be without difficulty. We think it would place more weight on the intellectual property legislation than that legislation is designed to bear. The provisions about registered IP do not have a coherent set of ranking rules: they have a few specific rules, but no general scheme. Moreover, they seem to presuppose that a security right will exist *before* any registration[70] and that would be inconsistent with the policy behind the statutory pledge, which is that it should not come into existence without satisfying the publicity principle.

22.48 Given that registration in the RSP should be fairly easy and inexpensive, we inclined in the Discussion Paper to think that no exception should be made, so that even if a statutory pledge were being granted solely over IP, it should still be registrable in the RSP.

22.49 Most consultees who responded to this question agreed, including the Faculty of Advocates, the Judges of the Court of Session, the Keeper of the Registers of Scotland and several law firm consultees. Others, notably Dr Ross Anderson, the Law Society of Scotland and Dr Hamish Patrick favoured registration in the relevant specialist IP register only.

22.50 We explored the issues here with our advisory group. A rule whereby a statutory pledge over registered IP would require to be registered in the relevant specialist register alone would only reduce time and cost where the statutory pledge was restricted to the IP. Thus, where a small business granted the statutory pledge over a patent and over equipment, there would have to be registration in the RSP because of the equipment being part of the subject matter of the statutory pledge.

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[68] Chapter 7.
[69] See paras 23.11–23.19 below.
[70] See, for example, Patents Act 1977 s 33(1) and Trade Marks Act 1994 s 25(3). But cf A Orr and T Guthrie, "Fixed Security Rights Over Intellectual Property in Scotland" [1996] 18 European Intellectual Property Review 596 at 597 and D P Sellar, "Rights in Security over 'Scottish Patents'" (1996) 2 Scottish Law and Practice Quarterly 137.

22.51 We doubt that a rule that the statutory pledge over registered IP is created by registration only in the relevant specialist register could be given effect without amendment being made to intellectual property legislation such as the Patents Act 1977. As we noted above, this legislation is reserved to the UK Parliament. At the moment it seems to us that the existing registration provisions concern *priority* of security rights rather than *constitution* of security rights. We understand also that in practice floating charges are not registered in the specialist registers and this too supports the view that registration is not constitutive.

22.52 In addition it is probable that a provision in our draft Bill requiring the statutory pledge to be constituted in a different way for registered IP than for other types of property would require legislation by the UK Parliament because IP law is a reserved area.

22.53 Legal advisers are familiar with having to register security documentation in more than one place given the requirements of the company charges registration scheme. In Chapter 36 below we consider in relation to that scheme that the ideal way forward would be an information-sharing arrangement, although this may be difficult to achieve in the short term. Our advisory group also supported that consideration be given to this as regards the RSP and the specialist IP registers. Once again we are aware that there are calls for a more radical reform of security rights over IP in the UK, for example, to have a unitary register, but that is beyond our scope given that it would require UK-wide legislation.[71]

22.54 We recommend:

97. In the case of registered intellectual property, registration of the statutory pledge in the relevant intellectual property register should not displace the requirement for registration in the Register of Statutory Pledges, but consideration should be given to establishing information-sharing arrangements between the registers.

Transferability

22.55 The enforcement of a security right involves the realisation of an asset, usually by it being sold.[72] Thus the asset requires to be transferable. We deal with the general requirement for transferability in Chapter 19 above, but the issue is particularly germane in the context of intellectual property. For example, "moral rights", being non-transferable,[73] could not be the subject of a statutory pledge. Some intellectual property licences can only be transferred under certain restrictions. Such assets could be encumbered by a statutory pledge, although clearly any prospective secured creditor would want to look closely at the relevant restrictions.

Enforcement

22.56 We deal with special issues as regards enforcement of a statutory pledge against IP in Chapter 28 below.

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[71] See S Thomas, "Security Interests in Intellectual Property" 2017 Legal Studies 214.
[72] See Chapter 28 below.
[73] Copyright, Designs and Patents Act 1988 s 94.

Other forms of incorporeal moveable property

Security over bank accounts

22.57 In England and Wales it is possible to create a charge over the credit balance in a bank account in favour of the bank with which the account is held.[74] This is known as a "chargeback". Under current Scottish law, the nearest equivalent is a so-called "pledge over account". Like the share pledge, this is misleadingly named, as it is actually an assignation.[75] The account holder is assigning its claim against the bank to the bank. Dr Anderson has noted that while in principle this creates the possibility of *confusio* (confusion),[76] there are good arguments that this doctrine is inapplicable, in particular because the assignation is only intended to be in security. He has also argued that an agreement providing for contractual set-off may have advantages over the pledge over account.[77]

22.58 If the statutory pledge were to be made available in respect of bank accounts similar difficulties as those discussed in relation to receivables above would require to be faced.[78] In other words, for there to be a "fixed security" within the meaning of the corporate insolvency legislation would seem to necessitate the secured creditor having "control" of the account. Given that (a) security can be achieved by assignation of the claim against the bank; (b) under our recommendations made above this could be achieved by registration in the RoA; and (c) the alternative possibility of contractual set-off, we are not convinced that there is a sufficient case for the statutory pledge to apply to bank accounts at this time. Of course it would be possible for the matter to be reviewed in the future.

Negotiable instruments

22.59 Negotiable instruments raise special issues. Thus in their consultation responses Brodies and the Law Society of Scotland noted that the Consumer Credit Act 1974 imposes restrictions on negotiable instruments being given in security in relation to a transaction regulated by that Act.[79] Earlier in this Report we recommended that negotiable instruments should be excluded from our proposed new scheme in relation to assignation of claims.[80] We understand from our advisory group that these are rarely used as collateral. Therefore, at least at the present time, we think that they should be excluded from the scope of the statutory pledge.

22.60 There is authority to the effect that negotiable instruments may be made the subject of a possessory pledge.[81] This whole area, however, is specialist and in our view it would add unnecessary complexity to our recommended new rules for possessory pledge to be

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[74] The leading case is *Re Bank of Credit and Commerce International SA (In Liquidation) (No 8)* [1998] AC 214. For discussion, see R Calnan, "Security over Deposits Again: *BCCI (No 8)* in the House of Lords" 1998 Journal of International Banking and Financial Law 125.
[75] See R G Anderson, "Security over bank accounts in Scots law" 2010 Law and Financial Markets Review 593 at 598.
[76] The doctrine that a person cannot hold a right against itself. See R G Anderson, "A Whimsical Doctrine: *Confusio*" in A J M Steven, R G Anderson and J MacLeod (eds), *Nothing so Practical as a Good Theory: Festschrift for George L Gretton* (2017) 31–45.
[77] Anderson, "Security over bank accounts in Scots Law" at 594–595 and 599–600.
[78] See paras 22.12–22.17 above.
[79] Consumer Credit Act 1974 s 123.
[80] See para 4.15 above.
[81] See Steven, *Pledge and Lien* paras 5-07 to 5-09.

made to apply to negotiable instruments. Further, this was not a subject on which we consulted. Therefore the provisions on possessory pledge in our draft Bill should apply to corporeal moveables (excluding money) only. We recommend:

98. Any rule of law in relation to a pledge over a negotiable instrument should be unaffected by the reforms recommended in this Report.

(Draft Bill, s 43(6))

Summary

22.61 In the table below we set out the possibilities for taking security over incorporeal moveable property if our recommendations are implemented.

Asset Type	**Statutory pledge**	**Security by transfer**
Claims (general)	No	Yes (by assignation)
Financial instruments (general)	Yes (with FCARs adaptations if appropriate)	Yes (by assignation with FCARs adaptations if appropriate or other form of transfer eg under the Stock Transfer Act 1963)
Intermediated securities	Yes (with FCARs adaptations if appropriate)	Yes (by assignation with FCARs adaptations if appropriate)
Intellectual property	Yes	Yes (by assignation, with registration in IP registers for registered IP)
Bank accounts	No	Yes (by assignation)
Negotiable instruments	No	Yes (by negotiation)

The future

22.62 The reasons why we recommend that the statutory pledge is restricted initially to financial instruments (including intermediated securities) and IP are set out above and are entirely pragmatic. We accept that the optimum position is for all incorporeal moveable property to be capable of being encumbered. But we consider that this must await future developments, in particular the review of corporate insolvency law. It would be sensible, however, to empower the Scottish Ministers to widen the classes of incorporeal property as and when they consider it appropriate to do so. We recommend:

99. The Scottish Ministers should have the power to prescribe other kinds of incorporeal moveable property over which a statutory pledge may be created.

(Draft Bill, s 47(2)(d))

Chapter 23 Statutory pledge: creation, amendment, transfer, restriction and discharge

Introduction

23.1 In this chapter we consider what is necessary for effective legal (juridical) acts in relation to a statutory pledge. First, we look at how this security right would be created. Secondly, we consider amendment and in particular adding property to the encumbered property and varying the secured obligation. Thirdly, we discuss transfer of statutory pledges by means of assignation. Finally, we consider how statutory pledges would be extinguished, in part by restriction, and in whole by discharge.

Creation

23.2 The creation of a statutory pledge, like the creation (or indeed transfer) of other rights in property in Scotland, would normally have three stages. First, there would be the contract between the prospective provider and the prospective secured creditor, known in most jurisdictions as the "security contract". Secondly, there would be the actual grant of the statutory pledge by the provider in favour of the secured creditor. Thirdly, there would be the creation of the real right in favour of the secured creditor. Only then would the statutory pledge be enforceable against third parties and in insolvency. In other words, only then would it truly be created. This contrasts with the attachment/perfection approach of UCC–9 and the PPSAs under which a security right is created on attachment but only has third party effect on registration. As discussed earlier in this Report,[1] consultees did not favour such an approach.

(1) *Security contract*

23.3 A security contract sets out the details of the security transaction including the rights and obligations of the parties, particularly in relation to when the security can be enforced. Strictly, there is no requirement for a contract prior to the grant of a right in security, in the same way as property can be transferred without a preceding contract of sale. But of course in commercial practice there is invariably a security contract. Such a contract will be in writing. We see no need for writing to be mandatory as the law generally only insists on writing for contracts relating to real rights in land rather than moveable property.[2]

[1] See paras 18.44–18.49 above.
[2] Requirements of Writing (Scotland) Act 1995 s 1(2)(a)(i).

(2) Grant of statutory pledge by means of constitutive document

23.4 The statutory pledge, like other non-possessory rights in security, should require a constitutive document.[3] There are a number of reasons why. The first is evidential. Possessory rights in security are evidenced by the secured creditor having possession of the encumbered property. With non-possessory rights in security the encumbered property remains with the provider and other evidence is needed to prove the existence of the right. The second reason is connected to the first. In the Discussion Paper we proposed that the new security right would be created in a similar way to a standard security, namely by the registration of a constitutive document.[4] As we shall see below,[5] this proposal was generally supported by consultees. Registration of a constitutive document obviously means that such a document is required. It would not be possible for a statutory pledge to be granted orally. Thirdly, where the provider of a statutory pledge is a company or LLP, Part 25 of the Companies Act 2006 means that the statutory pledge as a right in security would need to be registered in the Companies Register. Since 1 April 2013 the method is document registration.[6]

23.5 The constitutive document would require to be granted by or on behalf of the provider. The provider could sign a hard copy of the document in ink, or, to put this more formally, execute it as a traditional document in terms of the Requirements of Writing (Scotland) Act 1995.[7] Increasingly, of course, documents are signed electronically and this should also be possible. We think that the position should be the same as for assignation documents, discussed earlier in this Report,[8] namely that the Scottish Ministers should have power to modify what is required for signature by pen and ink (execution) and electronic signature (authentication) so that it is different from that required under the 1995 Act if they consider this is appropriate.[9]

23.6 There requires to be an exception for the need to sign the constitutive document where the encumbered property is a financial instrument and the FCARs[10] apply. We discuss this in Chapter 37 below.

23.7 The constitutive document would have to identify the encumbered property. That may be either property of, or property to be acquired by the provider, including property not yet in existence. As we saw in Chapter 20, consultees supported the ability of the statutory pledge to cover future assets.[11]

23.8 The level of identification would have to satisfy the specificity principle of property law,[12] in other words it would have to be sufficiently clear to allow third parties to determine

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[3] For example, for standard securities, see the Conveyancing and Feudal Reform (Scotland) Act 1970 Sch 2. For floating charges a document is also necessary because of the requirement for registration under the Companies Act 2006 Part 25.
[4] Discussion Paper, paras 20.15–20.20.
[5] See Chapter 29 below.
[6] See Chapter 36 below.
[7] Requirements of Writing (Scotland) Act 1995 ss 1A and 2.
[8] See para 4.23 above.
[9] This should also be the case as regards authentication for amendment and assignation documents, which are also discussed in this chapter.
[10] SI 2003/3226.
[11] As is the case in other jurisdictions. See eg the Belgian Pledge Act of 11 July 2013 art 13 (which provides for art 8 of the new Book III title XVII of the Civil Code).
[12] See Gretton and Steven, *Property, Trusts and Succession* paras 4.13–4.15.

which assets are covered. Whether the test is met would have to be determined on a case by case basis. Earlier we recommended, as a protective measure, that for consumer providers the asset should require to be specifically identified.[13] But for other providers it should be possible for items of encumbered property to be described in terms of their constituting an identifiable class such as "my computers" or "my vehicles" or "the computers to be listed on schedules to be sent" from the provider to the secured creditor.

23.9 The constitutive document should also require to state the secured obligation. Under the accessoriness principle,[14] without such an obligation there can be no security right.

23.10 We recommend:

100. (a) A statutory pledge should require a constitutive document.

(b) The constitutive document should require to:

(i) be executed or authenticated by the provider,

(ii) identify the property which is to be encumbered property (which may be either property of, or property to be acquired by, the provider), and

(iii) identify the secured obligation.

(c) If the encumbered property is to consist of more than one item the constitutive document should not have to identify each item separately provided that the document identifies the items in terms of their constituting an identifiable class.

(Draft Bill, s 46)

(3) Creation of real right by means of registration

23.11 In the Discussion Paper we considered whether registration should be required for the proposed new right in security over moveable property.[15] We noted that in different countries in the world there are both approaches, although registration is the commoner. Arguments against registration include that it adds expense and that if sales of moveable property do not require registration, neither should security rights over moveable property. A further argument is that a registration requirement adversely affects creditors who do not know about it. This argument, however, is much stronger where a UCC–9/PPSA approach is followed and any transaction functioning as a security right must be registered. This is not the approach of our recommended scheme. Moreover, secured creditors will normally be banks and other financial institutions who are invariably well-informed about the law of credit and security rights.

23.12 There are, in contrast, strong arguments in favour of registration. It helps third parties, in particular future potential lenders, to know the position. The transparency brought

[13] See paras 19.50–19.51 above.
[14] See paras 19.27–19.30 above.
[15] Discussion Paper, paras 16.13–16.17.

about by registration also reduces the scope for disputes. It thus facilitates non-possessory security, while at the same time protecting third parties.[16] In addition it reduces the scope for fraud. A debtor's statement that certain assets are unencumbered can be checked by inspecting the register. In the event of insolvency, registration makes it easier to ascertain what rights the various creditors have. The general effect is to promote economic efficiency. Furthermore, because of the digital revolution, registration can be done quickly and cheaply.

23.13 In the Discussion Paper we asked consultees whether they agreed that, if a new non-possessory security right were introduced, it should be on the basis of some type of public registration.[17] In the chapter entitled "Security over ordinary incorporeal moveable property (reform options)" we asked a similar question. This was whether consultees agreed that, if a new security right over claims is introduced, it should be created by registration.[18] While this second question is in principle superseded following our recommendation in Chapter 22 to limit the statutory pledge as regards incorporeal moveable property to financial instruments and intellectual property, the views of consultees at a general level continue to be of interest. The Discussion Paper did not ask for their views as regards financial instruments, but in relation to IP, as discussed above in Chapter 22, the approach was in favour of registration. There was, as we saw in that chapter, a question about registered IP as to whether the new security right should be registered in the RSP as well as the specialist IP register.[19]

23.14 With the exception of Chris Dun, all consultees who answered the question in relation to corporeal moveables agreed that registration should be required. Mr Dun stated that he did not favour public registration. In contrast, Brodies and the Law Society of Scotland believed that there were "advantages in a registration-based non-possessory security arrangement". Magdalena Raczynska stated that "a mechanism enabling third parties [to know] that security has been taken is necessary". Scott Wortley said: "If a new moveable security is introduced it should require publicity in order to give notice to third party purchasers and creditors in accordance with the publicity principle. The most effective way to give publicity is through registration."

23.15 A number of consultees made further helpful comments. The Law Society of Scotland mentioned the need to comply with the rules on financial collateral arrangements. This is discussed in Chapter 37 below. It expressed concern about any disruption of existing practices as regards financing of cars and security rights over IP. But such concerns seem predicated on a UCC–9/PPSA functional approach which is not the approach that we are taking. The Law Society of Scotland and several law firm consultees all raised the issue of the extent to which third party purchasers should take the encumbered property free of the security right notwithstanding the registration. We address that matter in Chapter 24.

23.16 The consultee responses to the question about registration of the new security right in respect of claims followed a similar pattern, with overwhelming support. An exception was Jim McLean who did not favour a new security right and instead proposed a new scheme based on reform of the law of assignation.

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[16] See A Duggan, "A *PPSA* Primer" (2011) 35 Melbourne University Law Review 865 at 867.
[17] Discussion Paper, para 16.17.
[18] Discussion Paper, para 18.17.
[19] See paras 22.44–22.54 above.

23.17 The predominant approach internationally now is for possession or registration to be required for rights in security over moveables to have third party effect. This is typified by the UCC–9/PPSA jurisdictions, as well by the DCFR and the UNCITRAL Model law. The new Belgian Pledge Act of 11 July 2013 takes a similar approach.[20] So too do the Law Commission for England and Wales in their recommendations in 2016 for new "goods mortgages".[21] We note also that one of the key objectives of the UNCITRAL Legislative Guide on Secured Transactions is "to enhance certainty and transparency by providing for registration of a notice of a security right in a general security registry."[22]

23.18 The jurisdictions which are perhaps most well-known for having laws of rights in security over moveable property which reject registration are Germany and the Netherlands. But these laws are increasingly coming under critical scrutiny. Alexander Morell and Frederic Helsen have argued that moving in the direction of the new Belgian register-based system would "be beneficial for the German system of non-possessory security interests. The higher the transparency in the system, the lower the cost of extending secured credit."[23] Dewi Hamwijk has compared Dutch law with the UCC–9 approach.[24] While she concludes that in practice Dutch law works reasonably well because of the low incidence of fraud, she sees benefit in a future European Register for Proprietary Security based on the DCFR Book IX if this can meet certain economic efficiency standards.[25]

23.19 We have concluded that registration should be required to create a statutory pledge.[26] In Chapter 29 below we discuss what exactly should be registered. We recommend:

101. Registration in the Register of Statutory Pledges should be a pre-requisite for the creation of a statutory pledge.

(Draft Bill, ss 48 to 49)

Creation and present assets

23.20 Where the statutory pledge is granted over property belonging to the provider, the secured creditor would obtain a real right on registration provided that the property is identifiable as encumbered property at time. This would be the moment that the statutory pledge is created over the property. For example, Eilish grants a statutory pledge in favour of Frederick over her Reubens painting. The statutory pledge is created on registration. It may be, however, that the encumbered property is not identifiable at the moment of

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[20] Belgian Pledge Act of 11 July 2013 art 20 (which provides for art 15 of the new Book III title XVII of the Civil Code). See F Helsen, "Security in Movables Revisited: Belgium's Rethinking of the Article 9 UCC System" (2015) 23 European Review of Private Law 959.

[21] Law Commission, Bills of Sale (Law Com No 369, 2016) ch 6.

[22] Available at https://www.uncitral.org/pdf/english/texts/security-lg/e/09-82670_Ebook-Guide_09-04-10English.pdf. See p 21.

[23] A Morell and F Helsen, "The Interrelation of Transparency and Availability of Collateral: German and Belgian Laws of Non-possessory Security Interests" (2014) 22 European Review of Private Law 393 at 437. In addition the authors refer at 436 to research that the introduction of a register-based system for security over movable property improves access to finance for businesses. See I Love, M S Martinez Peria and S Singh, "Collateral Registries for Moveable Assets: Does Their Introduction Spur Firms' Access to Bank Finance", World Bank Policy Research Working Paper (2013) available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2278093.

[24] Hamwijk, *Publicity in Secured Transactions Law.*

[25] Hamwijk, *Publicity in Secured Transactions Law* 372–374.

[26] Subject to an exception in respect of financial instruments because of the need to comply with the Financial Collateral Arrangements (No. 2) Regulations 2003 (SI 2003/3226) discussed in Chapter 37 below.

registration. If this is the case the statutory pledge would only be created on becoming so identifiable. For example, Vibrant Vehicles Ltd grants a statutory pledge in favour of Fochabers Funding Ltd over such of its vehicles as are set out in schedules to be delivered periodically to Fochabers Funding. The statutory pledge is duly registered but would only be created over a particular vehicle once it is identified in a schedule which is delivered. Thus the same statutory pledge would have different ranking points for different vehicles depending on when it was created over them. We discuss the issue of multiple ranking points further in the next section.

23.21 We recommend:

> **102. (a) A statutory pledge over property which, at the time the statutory pledge is registered, is the provider's and is identifiable as property to which the constitutive document relates, is created over that property on registration.**
>
> **(b) If the property is not yet so identifiable, the statutory pledge is created over that property on it becoming so identifiable.**
>
> (Draft Bill, s 48(1) & (2))

Creation and after-acquired assets: general

23.22 A statutory pledge could be granted over future assets.[27] Imagine that in May 2020 George grants a statutory pledge over "any motor vehicles present and future". The statutory pledge is registered in the RSP. In May 2021 George acquires a vintage Rolls Royce. At what point should the statutory pledge be created in respect of this vehicle?

23.23 Under the property law principle of *nemo plus*,[28] someone cannot give an effective right over property which is not theirs. On this approach the statutory pledge cannot be created in relation to the vehicle until George acquires it in May 2021. Thus the one statutory pledge may have several ranking points depending on when property is acquired.

23.24 The UCC–9/PPSA rules, however, are different and there is typically one ranking point: the moment of registration of the financing statement.[29] No distinction is therefore made between present and after-acquired property for this purpose. But, to achieve this, the registration requires to have retroactive effect (effect *ex tunc* as opposed to *ex nunc*). Other rules then have to be imposed to protect secured creditors who had security rights over the asset prior to it being acquired by the provider, but which post-date the registration.[30]

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[27] See para 23.7 above.

[28] In full, this is *nemo plus juris ad alium transferre quam ipse haberet* (nobody can transfer a better right than they have in the first place). It is also known by the shorter *nemo dat quod non habet.*

[29] Eg NZ PPSA 1999 s 66. For commentary, see Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 257–262.

[30] For example, X Ltd grants a security right over its vehicles present and future in favour of Bank B. This is registered in 2020. In 2025 it acquires a van from W Ltd. In 2022 W Ltd had granted a security right in favour of Bank A which was registered that same year. That security right is not extinguished (for example by a good faith acquisition rule) when the van is transferred to X Ltd. Bank A's security right was registered in 2022, but Bank B's security was registered before that in 2020. Nevertheless, Bank B clearly should have priority. Under the PPSAs a special rule is needed to achieve this. See eg the NZ PPSA 1999 s 88.

Registration may also precede the creation of the security right, but the priority point is registration.[31] The same is true under the DCFR Book IX.[32]

23.25 We are not persuaded to adopt the UCC–9/PPSA rules. While a traditional property law approach leads to different ranking points for the same statutory pledge, questions of priority would often be straightforward to resolve. Imagine that James, a sole trader, grants a statutory pledge over his van and any future vans to Bank A. This is registered in the RSP in 2020. He grants a second statutory pledge over the same assets to Bank B, which is registered in the RSP in 2021. Each year between 2021 and 2025 he acquires a new van. In 2026 he becomes insolvent. Bank A should have priority over Bank B in respect of all the vans, although the statutory pledges were only created in respect of the vans as they were acquired. In Chapter 26 we recommend a ranking rule to this effect, although it may well already be a general rule of rights in security law in Scotland.[33]

23.26 Thus we conclude that the statutory pledge should be created in respect of after-acquired property on that property being acquired, provided that the property is identifiable from the constitutive document or an amendment document[34] which has been registered. If the property is not so identifiable at that time then creation of the statutory pledge would not occur until it does become so identifiable. We gave the example above of Vibrant Vehicles Ltd granting a statutory pledge in favour of Fochabers Funding Ltd over such of its vehicles as are set out in schedules to be delivered periodically to Fochabers Funding. Imagine that a schedule is delivered which identifies a BMW that Vibrant Vehicles is about to acquire. On the acquisition subsequently taking place the statutory pledge is created over the BMW. But imagine that an Audi is acquired at the same time. It is only listed in a subsequent schedule. It is only on that subsequent schedule being delivered that the statutory pledge is created over the Audi.

23.27 We recommend:

> **103. A statutory pledge should be created over after-acquired property when that property becomes the provider's property, provided that the property is identifiable at that time as property which is to be encumbered property. If it is not so identifiable at that time then the pledge should not be created until such time as it does become so identifiable.**
>
> (Draft Bill, s 48(1) & (2))

Creation and after-acquired assets: insolvency of the provider

23.28 We consider that there should be a qualification to the general rule that a statutory pledge can extend to after-acquired assets. This is where the provider becomes insolvent after the statutory pledge is granted and the assets are acquired after that. Similar policy issues arise here as those discussed in Chapter 5 above in relation to assignation of future

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[31] Eg NZ PPSA 1999 s 146. For commentary, see Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 465–466.
[32] DCFR IX.–3:305(2) and 4:101(2)(a).
[33] Discussion Paper, para 16.53.
[34] We deal with amendment documents at paras 23.33–23.40 below.

claims.[35] Providers who have become insolvent should be entitled to a fresh start and not have new assets acquired by them taken away to satisfy pre-insolvency secured creditors. For assignation of subsequently arising claims we recommend a rule whereby an assignation is ineffective for claims arising after the commencement of an insolvency, except for claims in respect of income from assets. This enables assignations of income streams such as assignations of rents to remain valid.

23.29 For the statutory pledge we recommend a simpler rule that property acquired after the commencement of insolvency is not covered. In practice, we doubt that providers would acquire new corporeal moveables or financial instruments or intellectual property after they become insolvent because they would not have funds to do so. And of course while the insolvency is ongoing such assets would fall into the estate managed by the insolvency official. In a commercial context goods are typically sold subject to retention of title clauses and the provider will never become the owner if they cannot pay for them.

23.30 The same issues apply here as for assignation of future claims with regard to defining "insolvency".[36] Once again we have not had the advantage of formal consultation on the matter. We have therefore included in our draft Bill the same processes. We consider here too that the Scottish Ministers should have the power to amend the provisions by secondary legislation and we would expect the Scottish Government to consult on this matter as part of any future consultation on this Report.

23.31 In its response to our draft Bill consultation of July 2017 ICAS argued that we should recommend also a general rule that a statutory pledge is ineffective where it is created after the provider has become insolvent. It pointed to section 245 of the Insolvency Act 1986 but this provision is aimed principally at floating charges created within a certain period prior to the commencement of an insolvency.[37] Our view, however, is that this is a broader matter for insolvency law as to how the grant of a real right over moveable property owned by the grantor is affected where the real right is not acquired by the grantee before the insolvency commences. Thus the same question arises as regards the transfer of ownership of the property, or the grant of a liferent or a possessory pledge over it. We therefore do not favour a provision specific to statutory pledge. In contrast, we think that it should be put beyond doubt that although a statutory pledge is registered prior to the commencement of an insolvency it cannot extend to future assets acquired by the provider after that time.

23.32 We recommend:

104. (a) A statutory pledge granted prior to the provider becoming insolvent should not be able to encumber property acquired after that time.

(b) A provider who is an individual, or the estate of which may be sequestrated, becomes insolvent when:

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[35] See paras 5.105–5.109 above.
[36] See para 5.108 above.
[37] It also mentioned the Insolvency Act 1986 s 127, which is limited to windings up by a court and which provides that "any disposition of the company's property . . . made after the commencement of the winding up is, unless the court otherwise orders, void." It suggested that the provision is unlikely to apply because a statutory pledge is unlikely to be a "disposition". But in our Discussion Paper on *Sharp v Thomson* (SLC DP No 114, 2001) para 4.17 under reference to *Site Preparations Ltd v Buchan Development Co Ltd* 1983 SLT 317 we took the view that "disposition" should be interpreted broadly and would include the grant of security rights.

(i) the provider's estate is sequestrated,

(ii) the provider grants a trust deed for creditors or makes a composition or arrangement with creditors,

(iii) a voluntary arrangement proposed by the provider is approved, or

(iv) the provider's application for a debt payment programme is approved under section 2 of the Debt Arrangement and Attachment (Scotland) Act 2002.

(c) A provider which is not an individual becomes insolvent when:

(i) a decision approving a voluntary arrangement entered into by the provider has effect under section 4A of the Insolvency Act 1986,

(ii) the provider is wound up under Part 4 or 5 of the 1986 Act or under section 367 of the Financial Services and Markets Act 2000,

(iii) an administrative receiver is appointed over all or part of the property of the provider including the encumbered property, or

(iv) the assignor enters administration, ("enters administration" being construed in accordance with paragraph 1(1) and (2) of schedule B1 of the 1986 Act).

(d) The Scottish Ministers should have power to amend the definition of "insolvent".

(Draft Bill, s 51)

Amendment of statutory pledge

23.33 It may be that the provider and the secured creditor wish to vary the terms of the statutory pledge. Take the following example. Andrew grants a statutory pledge over a valuable painting in favour of Bronwyn in return for a loan. A few months later Bronwyn agrees to make a further advance in return for the scope of the statutory pledge being extended to include a second painting. Here is a second example. Inverdeveron Innovations Ltd grants a statutory pledge over its patents in favour of the Boyndie Bank. The constitutive document sets out that the bank may not enforce its security by means of granting licences of the patents. The parties subsequently agree to depart from this restriction. In both examples the statutory pledge requires to be amended.

23.34 We consider that in principle the amendment of a statutory pledge should require the same form of writing as the constitutive document itself. That is to say there should be an amendment document executed (signed with pen and ink) or authenticated (signed electronically) by the secured creditor and the provider.

23.35 In general we do not think that such a document should require to be registered, except where it adds property to the encumbered property or it varies the secured obligation to increase its scope, where the current scope is apparent from the entry.[38] A third party looking at the RSP should be entitled to see that the scope of the statutory pledge has been extended. Without registration being required in such circumstances the third party would be misled. In contrast where the secured obligation is defined by reference to other documents which are not registered there seems no benefit to be gained by requiring the register to be updated if the obligation is varied.

23.36 Where property is being added the situation is similar to a grant of the statutory pledge in respect of that property. The amendment document should require to describe the property to be added. That property might be present or future property of the provider.

23.37 As for the constitutive document of a statutory pledge we consider it essential only that the amendment document is executed or authenticated by the provider, rather than both parties. The secured creditor's assent to the extension of the statutory pledge would be given by it taking delivery of the document and registering it in the RSP.

23.38 Where property is being added the creation (and thus priority) point in respect of that property would be the time of registration of the amendment document provided that the property is then identifiable as being encumbered property. If it is not identifiable at that point then the statutory pledge would be created in respect of it when it becomes identifiable.[39] As regards after-acquired property the priority point would be the time of acquisition provided it is identifiable as encumbered property at that time. If it is not so identifiable at that time, then it would only be created on becoming so identifiable. We give an example of how this would work above.[40]

23.39 There should be separate rules on amendment where the FCARs apply and these are discussed in Chapter 37 below.

23.40 We recommend:

105. (a) The secured creditor and the provider should be entitled to amend a statutory pledge by means of an executed or authenticated amendment document.

(b) An amendment document which relates to the addition of property to the encumbered property must identify the property to be added. That property may either be property of, or property to be acquired by the provider.

(c) An amendment document by virtue of which only an amendment adding property to the encumbered property is made need not be executed or authenticated by the secured creditor.

(d) Where an amendment document relates to (either or both):

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[38] See also paras 29.15–29.21 below.
[39] See paras 23.20–23.21 above.
[40] See para 23.26 above.

(i) the addition of property to the encumbered property,

(ii) variation of the secured obligation, where the extent of that obligation is to be increased and its current extent is determinable from the entry alone

the statutory pledge should be amended only on registration of that document.

(e) On the amendment being registered in respect of additional property, the statutory pledge is created over that property provided that it:

(i) is identifiable as property which is to be encumbered property, and

(ii) is the property of the provider.

(Draft Bill, ss 49 and 60)

Transfer (assignation)

23.41 It should be possible for a statutory pledge to be transferred by the secured creditor to a third party. Such a transfer would be by assignation. Provisions on transfer of security rights over moveable property are typical in legislation or instruments elsewhere.[41] They can also be found in Scotland for other types of security right.[42] For example, a bank may wish to transfer its loans and security rights to one of its group companies.

23.42 We consider that an assignation should require a document executed or authenticated by or on behalf of the secured creditor. This is because a transfer is a significant act which changes the identity of the secured creditor.

23.43 Sometimes the parties to a statutory pledge may wish to restrict the possibility of assignation. We think that they should be able to do so by agreement.[43] In the interests of commercial flexibility, it is not necessary for writing to be insisted upon but we would expect in practice such an agreement to be evidenced by writing (including electronic documents).

23.44 For standard securities (which of course are over land) an assignation is ineffective without registration in the Land Register.[44] But assignation of a security right over moveables in other jurisdictions typically does not require registration. This is the position under UCC–9, the PPSAs and the DCFR Book IX where assignation takes place off-register. Where, however, there has been an assignation, the person identified as the secured creditor on the register is under a duty to tell enquirers who the assignee is.[45] To avoid receiving requests more generally for information in relation to the security right (discussed in Chapter 35 below), a secured creditor who has assigned may choose to update the

[41] See eg DCFR IX.–3:328.
[42] For standard securities, see the Conveyancing and Feudal Reform (Scotland) Act 1970 s 14.
[43] There is a parallel here with anti-assignation clauses in relation to claims. See paras 13.2–13.11 above.
[44] Conveyancing and Feudal Reform (Scotland) Act 1970 s 14(1).
[45] See eg DCFR IX.–3:320(3): "Where the security right has been transferred, the person registered as the secured creditor must disclose the name and contact details of the transferee".

register by means of a correction.[46] Under the company charges registration rules,[47] assignations of security rights ("charges") are not registrable.[48]

23.45 We have concluded in the light of such comparative authority that it should not be necessary for an assignation of a statutory pledge to be registered for it to be effective. For third parties what is most important is to discover whether the person searched against has granted a statutory pledge. The third party can ascertain whether there has been an assignation by contacting the party named as the secured creditor. Elsewhere we set out duties of the person registered as secured creditor in relation to information requests.[49] Of course there are other arguments in favour of requiring registration, such as certainty and preventing fraudulent ante-dating in the event of the assignor becoming insolvent. Banks and financial institutions rarely, however, are the subject of insolvency. We are not persuaded that there is a strong enough case to insist on registration.

23.46 There is statutory provision in relation to standard securities that where enforcement has begun prior to the assignation that the assignee can "step into the shoes" of the assignor and continue with the procedure rather than having to restart it.[50] We think that this should be the case for the statutory pledge too, subject to the express provision of the parties.

23.47 Once again there should be separate rules on amendment where the FCARs apply and these are discussed in Chapter 37 below.

23.48 We recommend:

106. (a) Except in so far as the provider and the secured creditor otherwise agree, a statutory pledge should be transferable by means of an assignation document executed or authenticated by the secured creditor.

(b) Subject to the provisions of the assignation document, the assignation should convey to the assignee entitlement to the benefit of any noticed served, or enforcement procedure commenced, by the assignor in respect of the statutory pledge before assignation.

(Draft Bill, s 59(1) to (2))

Restriction or discharge of statutory pledge

23.49 Where a statutory pledge covers several items of property the provider and secured creditor should be able to agree that certain items should be released from it. Often this would be where part of the secured debt is being repaid. And if the whole debt is repaid

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[46] See Chapter 33 below.
[47] See Chapter 36 below.
[48] See G L Gretton, "Registration of Company Charges" (2002) 6 EdinLR 146 at 172. The changes made to the rules with effect from 1 April 2013 have not altered the position.
[49] See Chapter 35 below.
[50] Conveyancing and Feudal Reform (Scotland) Act 1970 s 14(2)(c). Section 14(2)(a) and (b) give the assignee the full benefit of all corroborative or substitutional obligations for the debt or any part thereof and the right to recover payment from the debtor of all expenses properly incurred by the creditor in connection with the security. We are of the view that these would automatically transfer under a general principle of the law of assignation: *accessorium sequitur principale* (accessory rights follow the principal). But as regards enforcement we think that the position should be stated expressly.

what would be desired is that the statutory pledge is extinguished. We have already set out one way in which a statutory pledge can be extinguished in part or in whole and that is by the secured creditor consenting in writing to the transfer of the property.[51] Clearly, it should also be possible for the statutory pledge to be extinguished in part or whole even where property is not being transferred. As per the legislation on standard securities, we refer to extinction in part as "restriction" and in whole as "discharge".[52]

23.50 We consider that both restrictions and discharges should require writing. This could be by means of a hard copy document signed in ink.[53] But an electronic communication should also be permissible. In the interests of commerce there should not be a requirement for an electronic signature of the standard set down for authentication of electronic documents by the Requirements of Writing (Scotland) Act 1995 and which we recommend for the constitutive document of a statutory pledge.[54] That standard protects the provider whereas release of the property from the statutory pledge is in the provider's interest.

23.51 In line with the position in other jurisdictions we do not think that restrictions and discharges should require registration. The need to register before extinction would be a clog on commerce. Thus when we recommended earlier that the secured creditor could consent to a transfer and allow the transferee to take the property unencumbered we did not impose a registration requirement.[55] There are also several examples of circumstances where a registered security right can be extinguished off-register. The most important is where the security is for a fixed sum.[56] Another is where the encumbered property is destroyed, because clearly there can be no security right without property. Earlier we recommended that registration should be required for certain amendments which increased the extent of the secured obligation and encumbered property. Here the register needs to be updated to warn third parties taking rights over the provider's property. But where there is a restriction or discharge such a third party is not prejudiced because the scope of the statutory pledge is being decreased.

23.52 It must be necessary for there to be ways of correcting the RSP to give effect to the restriction or discharge of the statutory pledge which has taken place off-register, particularly so as the provider is not prejudiced by a stale entry. We deal with this later.[57]

23.53 Once more there should be separate rules on extinction where the FCARs apply and these are discussed in Chapter 37 below.

23.54 We recommend:

107. It should be possible to restrict a statutory pledge to part of the encumbered property or to discharge it by means of a written statement made by the secured creditor.

(Draft Bill, s 61(1))

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[51] See paras 20.37–20.45 above.
[52] Conveyancing and Feudal Reform (Scotland) Act 1970 ss 15 and 17.
[53] In the language of the Requirements of Writing (Scotland) Act 1995 s 1A, a "traditional document".
[54] And for amendments and assignations of statutory pledges. See paras 23.5, 23.34 and 23.42 above.
[55] See paras 20.37–20.45 above.
[56] *Cameron v Williamson* (1895) 22 R 393. For discussion, see A J M Steven, "Accessoriness and Security over Land" (2009) 13 Edin LR 387 at 410–413.
[57] See Chapter 33 below.

Summary of juridical acts and their interaction with the Register of Statutory Pledges

23.55 In this chapter we have set out how different juridical acts in relation to a statutory pledge are to be effected. We think that it would be helpful to summarise here how these interact with the RSP. Where a statutory pledge is created in the first place or its scope as to secured obligation or encumbered property is increased beyond what is set out in the constitutive document, there would require to be *registration*. This is because these acts have the potential to prejudice third parties and therefore require to be publicised. In contrast, there would be no requirement to register a juridical act which does not affect the scope of the statutory pledge (assignation) or which reduces its scope (restriction) or extinguishes it (discharge). These juridical acts would take place off-register. There must, however, be the facility to update the register so that it reflects reality. That is *correction*, which is described in Chapter 33. For example, if a business has granted a statutory pledge over its vehicles to a bank in security of a loan and the bank subsequently discharges the pledge because the loan is repaid, the business should be entitled to have the register cleared. This can be done by correction.

23.56 The following table sets out the respective routes for juridical acts in relation to a statutory pledge to enter the RSP.

	Registration	**Correction**
Creation	✓	x
Amendment (adding property or increasing secured obligation)	✓	x
Assignation	x	✓
Restriction	x	✓
Discharge	x	✓

Chapter 24 Statutory pledge: protection of third party acquirers of encumbered property

Introduction

24.1 Where a statutory pledge was created over the provider's property, the provider would remain owner of that property. This is because a statutory pledge would be a "true" security right.[1] The existence of such a security right does not prevent the provider from transferring the property to someone else, but the acquirer takes the property encumbered by the security right.

24.2 In the Discussion Paper, we considered the possessory pledge and gave the following example.[2] If Adam owns a bicycle and grants to Ella a possessory pledge, and he then sells it to Siegfried, Siegfried becomes owner, but subject to Ella's rights. In such a case there is no need to protect Siegfried, because Ella's possession provides the pledge with publicity. The law therefore does not give Siegfried protection.[3] For non-possessory security rights, however, the facts are different. If Adam still holds the bicycle there is nothing to put Siegfried immediately on notice of the existence of the security right. Thus there is a strong argument that, at least in certain cases, Siegfried should be protected and take the bicycle free of the security right.

24.3 The argument has two main strands: (1) fairness to the acquirer; and (2) economic efficiency. In relation to (1), the argument is not conclusive as a purchaser of moveable property is generally at risk that the seller does not have title. The goods may be stolen. *Caveat emptor.* In contrast, for land the Land Register can be checked and the seller's right to sell verified with a very high level of certainty.[4] But while there is no general register as to ownership of moveable property,[5] statutory pledges would be registered in the Register of Statutory Pledges. An acquirer could eliminate the risk by carrying out a simple on-line search.

24.4 In relation to (2), commerce requires in certain situations that transfer of moveable property should not be hindered by having to take the time (no matter how short) and expense (no matter how small) to check a register. At a more general level the issue is an example of a classic property law dilemma of choosing between two innocent parties who have suffered from the actions of another party. Here the secured creditor and the good faith acquirer are the innocent parties and the provider is the party who has acted improperly by dealing with the encumbered property without the creditor's permission. In its 2016

[1] See para 19.1 above.
[2] Discussion Paper, para 16.30.
[3] Other systems take the same approach. See eg UCC § 9–320(e).
[4] Of course, there may still be risks such as the seller impersonating the true owner and forging that party's signature on the disposition (deed of transfer). In that case, however, a good faith acquirer is entitled to indemnity from the Keeper where the Register is rectified. See LR(S)A 2012 ss 74 and 77.
[5] There are certain specialist registers, for example for intellectual property.

Report on Bills of Sale, the Law Commission for England and Wales recommend criminal liability in fraud for providers who sell assets subject to a proposed new "goods mortgage" who do not declare that the goods are mortgaged.[6] We do not make a similar recommendation as we consider that the matter is a more general one for the law of rights in security as a whole rather than for the law of statutory pledges alone.

24.5 Good faith acquisition rules in relation to statutory pledge can be broadly categorised under two headings. The first is where the acquirer should not be expected to check the RSP because of the circumstances in which the property is being acquired. This is the subject matter of this chapter. The second is where, even if the acquirer does carry out a check of the RSP against the seller, the search would not reveal the existence of the statutory pledge.[7] We consider this matter in Chapters 31 and 32 below.

When acquirers should not be expected to check the RSP: general

24.6 Legislation on security over moveable property in other legal systems generally protects buyers in certain cases on the basis that they should not be expected to check a register.[8] Parties other than buyers are typically not so protected. Thus, in particular, prospective secured creditors are expected to consult the register to see whether the prospective provider has already encumbered the property. Donees tend not to be protected on the basis that they have not given value and therefore do not suffer a financial loss from the asset turning out to be subject to a security right.

When acquirers should not be expected to check the RSP: a broad good faith protection?

24.7 In the Discussion Paper we tested the views of consultees by asking a number of questions in relation to when good faith purchasers should be protected.[9] The widest approach we suggested was based on that of the Murray Report.[10] It recommended that a buyer would take free if the buyer "is not aware that the property is subject to a moveable security or is aware that the property is subject to such a security but is not aware that such [contract of sale] is made without the prior written consent of the holder of the security having been obtained."[11] This had to be read with the proviso that "for the purposes of this section a third party shall not be held to be aware that property is subject to a moveable security by reason only that" it had been registered.[12] We noted that the overall effect of this would have been that a moveable security would have seldom affected good faith buyers.

24.8 This approach is wider than that taken under UCC–9 and the PPSAs where good faith buyers who acquire outwith the course of the seller's business are generally not protected. Nevertheless, the Law Commission for England and Wales in its Report on Bills of Sale recommends for the proposed new "goods mortgage" that private purchasers who act in good faith and without actual notice of the mortgage should take the goods

[6] Law Commission, Bills of Sale (Law Com No 369, 2016) paras 8.46–8.54.
[7] We acknowledge the contribution of Dr John MacLeod in relation to this categorisation.
[8] See later in this Chapter.
[9] Discussion Paper, para 16.47.
[10] See paras 18.18–18.22 above.
[11] Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 11(4)(c).
[12] Draft Floating Charges and Moveable Securities (Scotland) Bill, cl 11(5).

unencumbered by it.[13] This is narrower than the Murray Report because only private purchasers are protected.

24.9 Consultees generally did not support the wide approach of the Murray Report. Aberdeen Law School stated: "If all good faith buyers were protected, the eroding effect on any security right would be marked and this would affect the attractiveness of the system." The Faculty of Advocates had similar concerns. Magdalena Raczynska commented that such an approach "would diminish the role of the register". The Keeper said: "If it is considered that a security should be created by registration, then in the Keeper's view there should be a general assumption that "good faith" requires searches of the register whenever it would be reasonable to expect an acquirer to search."

24.10 In view of consultees' comments and the general position in other jurisdictions we conclude that the approach taken in the Murray Report is too wide.

Sale in the ordinary course of a business

Introduction and comparator legislation

24.11 A standard feature of legislation in other jurisdictions and of international instruments is that purchasers are protected where the sale is in the ordinary course of the seller's business. In the words of Drobnig and Böger:

> "Transactions conducted in the ordinary course of the transferor's business should be protected; it would constitute a major obstacle for commerce in general if parties could no longer have confidence in the possession of the goods by the transferor and if it were necessary to investigate whether any registered security rights . . . existed in these assets."[14]

24.12 For example, UCC–9 provides:

> "Except as otherwise provided in subsection (e), a buyer in ordinary course of business, other than a person buying farm products from a person engaged in farming operations, takes free of a security interest created by the buyer's seller, even if the security interest is perfected and the buyer knows of its existence."[15]

24.13 We note the following. First, subsection (e) is about security rights perfected by possession. Secondly, "buyer in ordinary course of business" is perhaps misleading, for what is meant is a person who buys in the ordinary course of the seller's business. Thirdly, "farm products" is a limited category including crops and livestock.[16] Fourthly, the protection is only against security interests created by the buyer's seller and not that party's predecessors. Fifthly, even although purchasers know about the security interest they are protected.

24.14 The relevant provision in the New Zealand PPSA is:

> "A buyer of goods sold in the ordinary course of business of the seller, and a lessee of goods leased in the ordinary course of business of the lessor, takes the goods free

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[13] Law Commission, Bills of Sale (Law Com No 369, 2016) paras 8.23–8.33.
[14] Drobnig and Böger, *Proprietary Security in Movable Assets* 689.
[15] UCC § 9–320(a).
[16] UCC § 9–102(34).

> of a security interest that is given by the seller or lessor . . . unless the buyer or lessee knows that the sale or the lease constitutes a breach of the security agreement under which the security interest was created."[17]

24.15 This provision protects lessees as well as purchasers, but under Scottish law a lease of moveable property is merely a contractual and not a property right. Like the UCC–9 provision, protection is limited to security rights created by the seller, but in contrast there is no protection where the purchaser knows that the sale is in breach of the security agreement. The Australian PPSA has a rule broadly equivalent to that of New Zealand.[18] The approach in the EBRD Model Law is more complex but to similar effect.[19] Likewise, the DCFR gives protection where "the transferor acts in the ordinary course of its business".[20] In such circumstances the mere fact that the security right is registered does not prevent the acquirer being regarded as a good faith acquirer and thus being protected by the good faith acquisition rules in the DCFR Book VIII. The protection is not limited to security rights created by the transferor. The Belgium Pledge Act of 11 July 2013 protects transferees if the transfer takes place in the ordinary course of the seller's business or where they acquire in good faith.[21] But transferees which are businesses are expected to check the register if the acquisition is not in the ordinary course of the seller's business and are not to be regarded as being in good faith if they fail to do so.[22]

Consultation

24.16 We asked consultees whether they agreed that buyers in the ordinary course of the seller's business should take free from the new registered non-possessory security right (the statutory pledge). Consultees generally agreed. For example, Professor Eric Dirix said: "The protection of buyers in the ordinary course of the seller's business is universally accepted." John MacLeod stated that "this should certainly be the case in respect of corporeal moveables. It is less clear that businesses which buy and sell incorporeals should be relieved of the obligation of checking the register. The case for ongoing commerce in incorporeals is much less clear than the case for ongoing commerce in corporeal moveables." We agree. We think that the rule should not apply to intellectual property and we propose a separate rule below for financial instruments.

24.17 Several consultees, however, qualified their agreement by reference to the issue as to whether the new security right was to be fixed or floating. Scott Wortley said: "General rules on the protection of the buyer are sensible, but if they go too far do they risk rendering the new security a floating rather than a fixed security?" Two law firm consultees[23] stated: "We see this as a critical consequence of the classification of the security as fixed or floating. If the intention (as we believe it should be) is to create a fixed security, the value of such a security would be limited by this provision. Our preference would be that an effective properly registered fixed security should prevail over buyers in the ordinary course [of

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[17] NZ PPSA 1999 s 53(1). See Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 220–231.
[18] Australian PPSA 2009 s 46. See C Wappett, *Essential Personal Property Securities Law in Australia* (2nd edn, 2013) 175–180.
[19] EBRD Model Law arts 19–21.
[20] DCFR IX.–6:102. See Drobnig and Böger, *Proprietary Security in Movable Assets* 689–691.
[21] See E Dirix, "The New Belgian Act on Security Interests in Movable Property" (2014) 23 International Insolvency Review 171 at 176.
[22] Belgian Pledge Act of 11 July 2013 art 30 (which provides for art 25 of the new Book III title XVII of the Civil Code).
[23] Dundas & Wilson and McGrigors.

business] unless the security holder has agreed otherwise." SCDI said: "For small and medium sized businesses, any requirement to have to search a register before carrying out a day to day commercial transaction would impose an additional burden on them which is unlikely to be helpful."

The statutory pledge as a fixed security

24.18 The Discussion Paper contemplated the new security right being either fixed or floating, but for the reasons set out in Chapter 20 above the statutory pledge is to be fixed only. The general rule outlined in that chapter is that the provider requires to obtain the consent of the secured creditor to specific transfers or the transferee will take the property still encumbered by the statutory pledge. The practical effect is that the statutory pledge is not suitable for stock-in-trade (inventory) except for the case of higher-value items where it is practical to obtain creditor consent to individual disposals. We gave the example of sales of high-value agricultural machinery.[24]

24.19 Thus because the statutory pledge is a fixed security and therefore not generally meant for stock-in-trade it might be concluded that there is no need for an "ordinary course of business" rule. It is instructive in this regard to look at the position in England and Wales. The current law is not entirely clear. A buyer for value and without notice will take free of an equitable security, such as a fixed charge.[25] The fact, however, that the charge is registered in the Companies Register could be argued to provide the buyer with constructive notice of it. Some take the view, however, that registration is only constructive notice to those who would be reasonably expected to check the register and this would not include buyers in the ordinary course of a business.[26]

24.20 The Report of the Law Commission for England and Wales on Company Security Interests[27] recommended "that a transferee (other than a secured party) of collateral that is subject to a registered charge which is a fixed charge should take subject to a charge unless the chargee has authorised the sale or other disposition."[28] This was on the basis that stock-in-trade would never be subject to a fixed charge. In its draft Secured Transactions Code of 2016, the Financial Law Committee of the City of London Law Society, following accounting terminology, draws a distinction between "current assets" (for floating charges) and "fixed assets" (for fixed charges).[29] Its proposed rule for fixed charges is that if these have been registered an acquirer does not take free of the charge.[30]

24.21 The difficulty, however, is that in some cases in particular for high-value assets it may actually be practical to trade in a way that consent from the secured creditor can be sought for individual disposals. Should a purchaser of a high-value piece of equipment from an equipment supplier realistically be expected to check the RSP? Moreover, there may also be cases where the provider does sell assets without obtaining the creditor's consent. Take the following example. A garage business grants the statutory pledge over its equipment for repairing vehicles. The business subsequently diversifies and becomes a supplier of such

[24] See para 20.49 above.
[25] Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 13.25.
[26] Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 12.05.
[27] Law Com No 296 (2005). See paras 4.25–4.31 above.
[28] Law Com No 296 para 3.218.
[29] City of London Law Society draft Secured Transactions Code, section 41.
[30] City of London Law Society draft Secured Transactions Code, section 43.1(b).

equipment. It does not obtain the secured creditor's consent to dispose of equipment subject to the statutory pledge. In these circumstances we consider that a good faith acquirer should be protected. We note too that the broad protection proposed by the Murray Report discussed above[31] was in the context of a fixed security.

24.22 It should be stressed that this rule could not be used to enable the statutory pledge to act as a floating charge by the secured creditor acquiescing in sales by the provider without obtaining the appropriate consent first. This is because of the recommendation which we made earlier that the effect of such acquiescence would be to extinguish the statutory pledge.[32]

Conclusion

24.23 We consider that there should be a general rule that a purchaser who takes corporeal property in the course of the seller's business should be protected despite the transfer being in breach of the requirement to obtain specific consent of the secured creditor, provided that the purchaser is in good faith. We think that the purchaser should take free of any statutory pledge granted by the seller, or the seller's predecessors, in line with the position under the DCFR and Belgian law.[33] Purchasers should not be in bad faith because they have not consulted the RSP.

24.24 We recommend:

> **108. (a) A person who purchases corporeal property which is encumbered property and which is, or has been transferred without the required consent of the secured creditor, should acquire it unencumbered by the statutory pledge if:**
>
> **(i) the person from whom the property is acquired is acting in the ordinary course of that person's business, and**
>
> **(ii) at the time of acquisition, the person is in good faith.**
>
> **(b) A person should not be taken to be other than in good faith by reason only of the pledge having been registered.**
>
> (Draft Bill, s 54)

Lower-value goods

24.25 In the Discussion Paper we noted that some jurisdictions and international instruments have provisions protecting good faith acquirers of lower-value goods, even where these are not acquired in the course of the seller's business.[34] The EBRD Model Law has a general rule to this effect,[35] but the rules in the Australian and New Zealand PPSAs

[31] See paras 24.7–24.10 above.
[32] See paras 20.52–20.53 above. This was a concern of R3 in its response to our draft Bill consultation of July 2017.
[33] For the counter-argument that protection should only be in respect of a statutory pledge granted by the seller see M Gedye, "The New Zealand Perspective" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 115 at 122.
[34] Discussion Paper, paras 16.37 and 16.45.
[35] EBRD Model Law art 21.2.5.

are restricted to consumer purchases. Thus in Australia the goods must be bought "predominantly for personal, domestic or household purposes".[36] The threshold figure is currently A$5,000 (about £2,911). In New Zealand the provision applies to goods acquired as "consumer goods"[37] and this term is defined as "goods that are used or acquired for use primarily for personal, domestic, or household purposes".[38] The threshold figure is currently NZ$2000 (about £1,048) which is lower than the Australian figure. The New Zealand figure is based on the value of the goods at the time that the security right attached (in effect was created), whereas the Australian figure is based on the value given by the acquirer. Both provisions require "new value" to be given. The reason for that is because under these systems security rights extend to proceeds.[39] The New Zealand approach can be criticised for being based on a historic rather than current value of the goods.[40] Both provisions enable the acquirer to take free of all security interests, whether created by the seller or another party.

24.26 We asked consultees whether there should be a rule that a good faith buyer should always take free from the new security right where the price paid by the buyer is below a certain limit (to be adjusted from time to time by statutory instrument). We asked also what the limit should be. Consultees were divided on this matter, with a majority inclining against such a rule. Two law firm consultees[41] stated: "We do not believe such a rule is appropriate: many transactions deal with a very large number of small value assets eg debts and a *de minimis* rule would require very careful consideration." The Law Society of Scotland, in a response in similar terms to that of the law firm, Brodies, said: "As the advantage associated with this form of security will be in dealing with large portfolios of relatively small value assets [we are] not sure that such a *de minimis* rule would be helpful. Individual sales below the prescribed limit could quickly erode the value of such security." On the other hand, the WS Society favoured a wider approach following the Murray Report[42] that any good faith buyer should be protected.

24.27 We agree that there should be no rule of general application here. But we are persuaded that as in Australia and New Zealand good faith private purchasers (or acquirers otherwise giving value) should be protected in the case of lower-value goods where these are wholly or mainly acquired for personal, domestic or household purposes. This protection would only apply to corporeal moveables. Take the following example. John is a sole trader gardener. He owns five lawnmowers which he uses for varying types of lawns. He does not trade in lawnmowers. He grants a statutory pledge over his business equipment including the lawnmowers and therefore the protection rule outlined in the previous section would not apply. He subsequently sells one of the lawnmowers to Jean for £500 without the secured creditor's permission. Jean is in good faith. We think that she should be protected.

24.28 There is then the issue of where the threshold should be set. In his response, John MacLeod argued that "it might be better if the test was not of the price paid by the buyer but the value of the goods to avoid complications where the price of the goods was deliberately set below the ceiling". We agree.

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[36] Australian PPSA 2009 s 47(2).
[37] NZ PPSA 1999 s 54.
[38] NZ PPSA 1999 s 16(1).
[39] See Australian Statutory Review 2015 para 7.6.1.1.
[40] See Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 232.
[41] Dundas & Wilson, and McGrigors.
[42] See paras 24.7–24.10 above.

24.29 The figure should be set by statutory instrument. Aberdeen Law School suggested £1,000. Dr Ross Anderson made an "arbitrary" suggestion of £5,000. These were the only two specific suggestions. We think that the figure should be at least £1,000. When setting it we think that the Scottish Ministers should have regard also to the threshold figure below which a corporeal asset owned by an individual not acting in the course of a business cannot be made the subject of a statutory pledge.[43] This would effectively prevent the rule recommended here operating in consumer-to-consumer sales. Thus if a private individual can only grant a statutory pledge over assets each worth more than £1,000 and the low-value goods acquisition protects goods with a value less than £1,000 then it cannot come into play as regards statutory pledges granted by private individuals.

24.30 We consider also that this rule should not apply to motor vehicles, for which we recommend a separate rule below.[44] We recommend:

109. (a) An individual who acquires corporeal property which is encumbered property and which is, or has been, transferred without the required consent of the secured creditor, should acquire it unencumbered by the statutory pledge if:

(i) the value of all that is acquired does not, at the time of acquisition, exceed such amount (if any) as the Scottish Ministers may by regulations specify,

(ii) at the time of acquisition, the acquirer is in good faith,

(iii) the acquirer gives value for the property acquired, and

(iv) the property is wholly or mainly acquired for personal, domestic or household purposes.

(b) This rule should not apply in respect of the acquisition of encumbered property (or any part of that property) which consists of a motor vehicle.

(c) A person should not be taken to be other than in good faith by reason only of the pledge having been registered.

(Draft Bill, s 55)

Relevance of delivery

24.31 Under sections 24 and 25 of the Sale of Goods Act 1979 (the rules on sellers and buyers in possession), a pre-condition for the protection of the buyer from the seller's lack of title is that the goods have been delivered to the buyer. We noted in the Discussion Paper that this approach is not generally to be found in UCC–9 and the PPSAs but we asked consultees whether it should be a requirement for protection in Scotland.[45]

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[43] See paras 19.36–19.51 above.
[44] And motor vehicles would typically have a higher value than the threshold figure in any event.
[45] Discussion Paper, para 16.46.

24.32 The responses which we received generally did not favour delivery. For example, Aberdeen Law School, in a thoughtful response,[46] stated:

> "The interaction with s 17 of the Sale of Goods Act 1979 (as amended) would need to be considered carefully. If delivery is the step at which security is purged, yet ownership is transferred earlier by agreement, a buyer would need to undertake two steps rather than one to acquire unencumbered ownership.
>
> This two-step process is something that has been alien to Scots law since the Sale of Goods Act 1893. The case for delivery has not been made, and the analogy with sections 24 and 25 of the Sale of Goods Act 1979 is imperfect . . . when transfer can happen without delivery it would be bizarre to leave a security right attached after the seller has divested itself of the asset."

24.33 Consultees including Dr Hamish Patrick, the Law Society of Scotland and several law firms suggested payment of the price as a pre-requisite for protection. We agree. Thus the "in the course of a business" and "lower-value goods" protections set out above both require payment to be made/value given but not delivery.

When acquirers should not be expected to check the RSP: motor vehicles

24.34 The current lack of a non–possessory security over moveable property in Scotland is one of the reasons why hire-purchase contracts are popular. Typically what happens is that a supplier sells the goods to a finance company which then enters into a hire-purchase contract with the customer. This is a contract of hire, but with a purchase option which the buyer can choose whether or not to exercise.[47] In contrast, in a conditional sale transaction the customer does acquire ownership on paying all the instalments.

24.35 Until the option is exercised, ownership of the goods remains with the finance company. Therefore if the customer sells the goods, the purchaser does not acquire ownership. The Hire-Purchase Act 1964, however, provides an exception for private purchasers who have acted in good faith, but only in relation to motor vehicles.[48] The protection also applies where the motor vehicle is the subject of a conditional sale.

24.36 A statutory pledge over a motor vehicle would be functionally similar to hire-purchase or conditional sale. The customer would have possession of the vehicle. But rather than it being owned by the finance company, the customer would grant a statutory pledge over it which would be registered in the RSP. We are of the view that good faith private purchasers should be protected under the same principles in the 1964 Act. Some of its provisions are not particularly easy to follow and we have therefore tried to take a simpler approach.[49]

24.37 First, we think that the same definition of "motor vehicle" should be used, namely "any mechanically propelled vehicle intended or adapted for use on roads to which the public has access".[50] Secondly, the vehicle should be the subject of a statutory pledge. Thirdly, there should be a sale agreement, conditional sale agreement or hire-purchase agreement made in respect of the vehicle.[51] Fourthly, the purchaser or hirer, at the time of entering into

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[46] Authored by the late Professor David Carey Miller.
[47] See the definition in the Consumer Rights Act 2015 s 7.
[48] Hire-Purchase Act 1964 s 27.
[49] We note also in this regard Law Commission, Bills of Sale (Law Com No 369, 2016) paras 8.55–8.58.
[50] Hire-Purchase Act 1964 s 29(1)(b).
[51] This follows from the definition of "disposition" in the Hire-Purchase Act 1964 s 29(1).

the agreement should be in good faith.[52] They should not have to check the RSP in order to satisfy this test. Fifthly, the purchaser or hirer should not be a person carrying on a business which is described in section 29(2) of the 1964 Act. In other words, the person must not be a trade or finance purchaser ie not someone who carries on a business involving trading in motor vehicles or providing finance for their hire-purchase or conditional-sale. The result is that many business purchasers (not being motor dealers) are protected.[53]

24.38 On these conditions being satisfied the purchaser or hirer should obtain the motor vehicle unencumbered on it being transferred. In the case of conditional sale and hire-purchase, however, the transfer would not be immediate. It would only happen on the relevant conditions being satisfied or on the hirer exercising the option to acquire the property. In the meantime it should not be possible for the statutory pledge to be enforced against the vehicle.

24.39 We consider also that where the party who sells or hires the motor vehicle is a trade or finance purchaser they should be liable to the secured creditor for the lesser of the amount remaining due under the secured obligation and the amount received, or to be received in respect of the transfer. We have been influenced in this regard by section 59 of the NZ PPSA 1999, but section 27(6) of the 1964 Act rather more opaquely would seem to impose similar liability. The policy is that trade or finance purchasers should exercise a higher standard of care when dealing with vehicles. Take the following example. Louise grants a statutory pledge over her van in favour of the Ballantrae Bank. The security right is registered in the RSP. Without the consent of the bank she sells the van to a motor dealership. The motor dealership subsequently sells to Joshua, who is in good faith. He acquires the van unencumbered by the statutory pledge. The motor dealership then becomes liable to the bank for the price it received or Louise's outstanding debt if lower. The motor dealership should have searched against Louise in the RSP prior to buying her van.

24.40 Finally, we believe that the Scottish Ministers should have the power to specify motor vehicles or classes of motor vehicle which are not to benefit from the rule. Our thinking here is that the RSP might in the future become so easy to check electronically that acquirers or certain classes of acquirer could be expected to check it. This may depend on the extent to which the registration of VINs (vehicle identification numbers) becomes compulsory.

24.41 In New Zealand there is a text message system known as "TXTB4UBUY". The NZ Personal Property Securities Register website states: "Before you buy a second hand vehicle, text us to check if money could be owing on the vehicle. There are three basic steps to completing a TXTB4UBUY search. First you send us an SMS text. Next you will receive a reply containing information that you then use to complete your search online. It costs $3 per submitted search (the fee is charged to your mobile phone) . . . You should receive an SMS reply within minutes."[54] In New Zealand good faith private purchasers from licensed motor dealerships are protected,[55] but purchasers from private individuals are expected to check the register.

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[52] See the Hire-Purchase Act 1964 s 27(2). This provision requires "good faith without notice" but we are not convinced that "without notice" adds anything.
[53] See W C H Ervine, *Consumer Law in Scotland* (5th edn, 2015) para 3-41.
[54] See http://www.ppsr.govt.nz/cms/searching-the-ppsr/txtb4ubuy.
[55] NZ PPSA 1999 s 58.

24.42 We note also that the Law Commission for England and Wales in its Report on Bills of Sale has recommended that new legislation introducing "goods mortgages" should contain a regulation-making power to repeal the protection which is to be given to good faith private purchasers of vehicles if vehicle provenance checks become free (or almost free) and a routine part of buying a second-hand vehicle.[56]

24.43 We recommend:

110. (a) The following rule should apply where:

(i) there is a sale agreement (or conditional sale agreement) or a hire-purchase agreement in respect of a motor vehicle,

(ii) the motor vehicle is encumbered property,

(iii) the purchaser or hirer is, at the time of entering into the agreement, in good faith, and

(iv) at that time the purchaser or hirer is not a person carrying on a business described in section 29(2) of the Hire-Purchase Act 1964.

(b) On the motor vehicle being transferred to the purchaser or hirer in accordance with the agreement, that person should acquire it unencumbered by the statutory pledge.

(c) And the statutory pledge should not be able to be enforced against the motor vehicle while the agreement is extant, and before the vehicle is transferred to the purchaser or hirer.

(d) But if the transferor is, at the time the agreement is entered into, a person carrying on a business described in section 29(2) of the Hire-Purchase Act 1964, the secured creditor should be entitled to receive from the transferor the lesser of:

(i) the amount outstanding in respect of the secured obligation, and

(ii) the amount received, or to be received, by the transferor in respect of the acquisition.

(e) A purchaser should not be taken to be other than in good faith by reason only of the statutory pledge having been registered.

(f) "Conditional sale agreement", "hire-purchase agreement" and "motor vehicle" should have the meanings given to those expressions by section 29(1) of the Hire-Purchase Act 1964.

[56] Law Com No 369, 2016 paras 8.37–8.45.

(g) The Scottish Ministers should have the power to make regulations specifying the motor vehicles, or classes of motor vehicle, to which these rules are not to apply.

(Draft Bill, s 56)

Financial instruments

24.44 In the Discussion Paper we said that it would be unacceptable if the new security right were to cause problems for the free marketability of shares.[57] This principle applies generally to financial instruments, such as corporate and public-sector bonds. We noted that there are different types of case. Dealers trading in shares on the London Stock Exchange cannot be expected to check the RSP. But if a member of a small private company sells shares in that company to another member, the position is arguably different and the buyer might be expected to check the register in those circumstances.

24.45 We canvassed two main options, with the second having sub-options. The first main option would be for good faith acquirers always to take free of a statutory pledge. The second would be to protect some good faith acquirers, but not others. For example, open-market buyers could be protected.

24.46 Consultees generally favoured protection for publicly tradeable financial instruments only. Thus Dr Ross Anderson argued: "There is no reason for protection to apply to shares in a company whose securities are not listed on a publicly traded exchange. In such cases, the buyer's professional advisers can be expected to check the RSP." The Law Society of Scotland and several law firm consultees doubted that the statutory pledge would be used for tradeable financial instruments because the need to protect good faith third party acquirers meant that the security right would be easily lost. It is worth remembering, however, that the statutory pledge would remain effective against transferees other than good faith buyers as well as against subsequent security rights and in the event of the provider's insolvency.

24.47 Following discussion with our advisory group, we have concluded that a good faith acquisition rule should apply to financial instruments on financial markets specified by the Scottish Ministers in regulations. This would allow flexibility because the situation in practice may change. We consider that acquirers should be protected if they do not know about the statutory pledge and the acquisition takes place in accordance with the rules of the specified financial markets. This is more generous than the earlier rules outlined in this chapter to protect acquirers. First, only actual knowledge by the acquirer of the statutory pledge would preclude the rule applying, and not a lack of good faith. Second, there would be no requirement to give value. The reason for this approach is the need to ensure free trading of financial instruments in financial markets.

24.48 We recommend:

[57] Discussion Paper, para 19.6.

111. (a) The following rule should apply where:

(i) a person, in the ordinary course of trading on a specified financial market, acquires a financial instrument of a specified kind, and

(ii) that financial instrument is encumbered property.

(b) The person should acquire the instrument unencumbered by the statutory pledge provided that:

(i) at the time of acquisition the person does not know of the statutory pledge, and

(ii) the acquisition takes place in accordance with the rules of the specified financial market.

(c) "Specified" should mean specified, for these purposes, by the Scottish Ministers by regulations.

(d) The regulations should be able to specify different markets or descriptions of market in relation to different kinds of financial instrument.

(Draft Bill, s 57)

Chapter 25 Possessory pledge

Introduction

25.1 This chapter considers reforms to possessory pledge, the consensual security over corporeal moveable property created by delivery which is recognised by the current law and also under our recommended new statutory regime. While, as we noted in the Discussion Paper,[1] there is more pressure for reform in relation to non-possessory security, we consider that some reform of possessory pledge is desirable. This was supported by consultees.

Delivery

25.2 Pledge under the current law is a possessory security.[2] The relevant property must be delivered to the secured creditor in order to satisfy the publicity principle[3] and to restrict the provider's ability to deal with the property. Thus while in principle the provider can still sell the property to a third party, the third party is warned of the existence of the pledge by the fact that the provider does not have direct possession of the property.

25.3 A preliminary point is that the *nemo plus* rule applies in relation to the creation of a pledge as it does to creation of other real rights. If the provider of the pledge does not own the property being pledged then no real right will be acquired by the secured creditor. But if the provider subsequently becomes owner of the property, although there is an absence of authority on the matter, we think that the pledge would then be created.[4] This would effectively be the same rule as for statutory pledge.[5] We therefore recommend that provision is made on the matter, although we doubt that this situation would commonly arise. Under English law it is possible for a pledgee to re-pledge the property. This is known as a "sub-pledge".[6] Scots law is otherwise.[7]

25.4 We noted earlier in this Report that the law recognises various types of delivery.[8] For pledge, however, the case of *Hamilton v Western Bank*[9] states that there must be actual delivery, in other words, the property has to be physically handed over to the creditor. The decision has been the subject of significant criticism and subsequent case authority casts doubt on it.[10] A court would hopefully take a different approach if the matter were to come before it today. For, if *Hamilton* is correct, this means that other forms of delivery cannot be used to create a pledge. Thus goods in a warehouse belonging to an independent third

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[1] Discussion Paper, para 15.2.
[2] See generally, Steven, *Pledge and Lien*. The present Report recommends the introduction of a new type of pledge, known as a "statutory pledge".
[3] On the publicity principle, see Discussion Paper, Chapter 11.
[4] This in effect is the doctrine of accretion.
[5] See para 23.27 above.
[6] The leading case is *Donald v Suckling* (1866) LR 1 QB 585.
[7] See Steven, *Pledge and Lien* paras 6-52 to 6-64. And see also the Belgian Pledge Act of 11 July 2013 art 19 (which provides for art 14 of the new Book III title XVII of the Civil Code).
[8] See para 17.18 above.
[9] (1856) 19 D 152.
[10] See para 17.18 above. In particular, *North-Western Bank Limited v Poynter, Son, & Macdonalds* (1894) 22 R (HL) 1, [1895] AC 56 and discussed below at para 25.11, is contrary to *Hamilton.*

party may be delivered constructively by intimation to the third party.[11] Goods aboard a ship may be delivered by means of handing over the bill of lading which represents them.[12] If such other methods of delivery are doubtful for possessory pledge, it makes the law unduly restrictive and puts barriers in the way of businesses wanting to use assets for security. For example, in Scotland whisky is kept in warehouses belonging to third parties, which makes it a suitable subject for security.

25.5 In English law it is clear that delivery is not limited to actual delivery. In *Sewell v Burdick*[13] the House of Lords decided that a pledge of a bill of lading is valid, the reason being that a bill of lading represents the civil possession[14] of the goods in question, but does not necessarily represent their ownership. In the Discussion Paper we stated our view that the English approach is clearly preferable. There is no reason why the transfer of possession of a bill of lading for the purpose merely of security should result in transfer of ownership, any more than when possession of a gold ring is transferred to a pawnbroker, ownership should pass. We considered that *Hamilton* represents an unjustifiable interference with the intentions of the parties and the commercial realities of the situation. We asked consultees whether legislation should bring Scots law into line with English law (as settled in *Sewell v Burdick*) by providing that the pledge of a bill of lading (or delivery order[15]) is a true pledge. All the consultees who responded to this question agreed, as did the Scotch Whisky Association when we informed them of our proposal.

25.6 We think that it would be helpful for the new legislation to set out the forms of delivery which are permissible. In the first place, it should clearly continue to be possible to pledge corporeal moveables by physically handing these over to the secured creditor or to a person authorised to accept delivery on that person's behalf. Larger items such as vehicles may not be physically handed over as such but rather control may be given to the secured creditor perhaps by means of keys.[16] Secondly, it should be competent for goods in a particular location to be pledged by giving the secured creditor, or a person authorised to act for that party, control of the location. The usual way to do this would be to hand over the keys to the relevant location, such as a store.[17] Thirdly, constructive delivery by instructing an independent third party holder of the property to hold it on behalf of the secured creditor, or that party's authorised representative, should also be possible. As mentioned above, the usual case is goods held in a warehouse. In English law this type of delivery (which is known as "attornment") requires the custodier to tell the secured creditor that the property is now being held for that party.[18] But this is not necessary in Scotland.[19] Fourthly, pledge by

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[11] *Anderson v McCall* (1866) 4 M 765; *Inglis v Robertson & Baxter* (1898) 25 R (HL) 70.
[12] See Carey Miller with Irvine, *Corporeal Moveables* para 8.27.
[13] (1884) LR 10 App Cas 74.
[14] Civil possession, otherwise known as indirect possession, means possession through another party. For example, the owner of goods which are in a warehouse has civil possession of them through the warehouse owner.
[15] In other words a delivery order issued by a custodier such as warehouse. There would require to be intimation to the custodier here for the pledge to be valid, contrary to the position with bills of lading.
[16] A point made to us by Dr Craig Anderson.
[17] Justinian, *Institutes* II,1,45. See too Reid, *Property* para 620 (W M Gordon). For English law, see Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 5.33.
[18] Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 5.25.
[19] Except under the Sale of Goods Act 1979 s 29(4). See Reid, *Property* para 620 (W M Gordon) and C Twigg-Flesner, R Canavan and H MacQueen (eds), *Atiyah and Adams' Sale of Goods* (13th edn, 2016) 103–104. See also C Anderson, "Delivery of Goods in the Custody of a Third Party: Operation and Basis" (2015) 19 EdinLR 165. Dr Anderson argues that delivery here can be analysed as the owner assigning its right against the holder, but this assignation is within a specific context. Thus the general rules of intimation discussed in Volume 1 of this Report seem inapplicable.

means of handing over a bill of lading[20] should be available, as it is under English law. Where the bill is an order bill of lading it would require to be endorsed in favour of the secured creditor.[21]

25.7 We do not favour allowing pledge by means of *constitutum possessorium* (delivery by act of mind alone whereby the property remains in the possession of the provider of the pledge).[22] This gives insufficient publicity to third parties and does not adequately restrict the provider's ability to deal with the property.[23]

25.8 Where the prospective encumbered property is already in the direct possession or custody of the secured creditor, the requirement for delivery is unnecessary.[24] Imagine that Neil has lent Olive his van. He then borrows £5,000 from her. Neil and Olive should be able to agree that the van can be pledged for the debt without it having to be redelivered back to Neil so that he can make a fresh delivery to Olive.

25.9 Finally, the new legislation requires to be made subject to section 2 of the Factors Act 1889,[25] which allows a mercantile agent to pledge goods in that party's possession. The 1889 Act goes on to provide that this may be done by means of a pledge of the "documents of title" to the goods.[26] "Documents of title" are provided to include any bill of lading, dock warrant, warehouse keeper's certificate, and warrant order for the delivery of the goods.[27] This seems to override the usual rule for constructive delivery that intimation to the warehouse is required.[28]

25.10 Accordingly we recommend that:

112. (a) For a possessory pledge to be created the property delivered must be or become the property of the provider.

(b) The rule in *Hamilton v Western Bank*, that pledge is restricted to actual delivery of the property which is to be encumbered, should no longer have effect.

(c) Delivery of corporeal moveable property in order to pledge it should be effected by:

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[20] The bill of lading is the only clear example of a document symbolising goods, so that delivery of it is equivalent to delivery of the goods. One of our advisory group members suggested an air waybill as another example, but while the position is not entirely clear it would seem that it is not. We considered widening the rule to cover "any document representing the property" but consultees to our draft Bill consultation of July 2017 criticised this approach on the basis that it was too uncertain.

[21] R M Goode, *Commercial Law* (5th edn, by E McKendrick, 2016) para 32.53.

[22] For discussion, see Carey Miller with Irvine, *Corporeal Moveables* paras 8.23–8.25.

[23] As has been noted in South Africa. See H Mostert and A Pope (eds), *The Principles of the Law of Property in South Africa* (2010) 317.

[24] The Romans referred to this as delivery *brevi manu.* See Reid, *Property* para 622 (W M Gordon).

[25] Applied in Scotland by the Factors (Scotland) Act 1890. See L J Macgregor, *The Law of Agency in Scotland* (2013) para 3-07.

[26] Factors Act 1889 s 3.

[27] Factors Act 1889 s 4.

[28] See Steven, *Pledge and Lien* para 9-34. See also Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 5.34.

(i) physically handing over or giving control of the property to the secured creditor or to a person authorised to accept delivery on behalf of the secured creditor,

(ii) giving control of the premises in which the property is located to the secured creditor or to a person so authorised,

(iii) instructing an independent third party who has direct possession or custody of the property to hold the property on behalf of the secured creditor or of a person so authorised, or

(iv) delivering a bill of lading to the secured creditor or to a person so authorised (and where that bill is to the order of a particular person, by effecting the endorsement of the bill in favour of the secured creditor).

(d) Property already in the direct possession or custody of the secured creditor or of a person authorised to hold the property on behalf of the secured creditor when agreement on the creation of the pledge is reached between the provider and the secured creditor is deemed to have been delivered to the secured creditor for the purpose of creating a pledge.

(e) These rules should be without prejudice to section 2 of the Factors Act 1889 (powers of mercantile agent with respect to disposition of goods).

(Draft Bill, ss 45 and 118(4))

Redelivery of pledged property for the purpose of sale

25.11 In *North-Western Bank Limited v Poynter, Son & Macdonalds*[29] a bill of lading was pledged to the bank, but returned to the pledger for the purposes of selling the goods. The provider of the pledge undertook to hold the goods in trust for the bank. The validity of this arrangement was challenged. The case proceeded in the Scottish courts and ended up in the House of Lords, where it was held to be subject to English law.[30] The decision was that the pledge survived the transfer back to the provider. It has come to form the legal basis of trust receipt financing. But what exactly is held in trust is not clear.[31] Thus if A pledges a bill of lading to B and B then hands it back on trust, A is now the trustee and owner of the goods. This suggests that B, as the beneficiary of the trust, is no longer a pledgee. Perhaps the law is that the pledge remains over the goods not sold and the trust covers the proceeds of those sold.

[29] (1894) 22 R (HL) 1, [1895] AC 56. See also the earlier decision in *McDowal v Annand and Colhoun's Assignees* (1776) 2 Pat 387.
[30] Both the pursuers and the defenders were English, but the case arose because of the arrestment of sums owned by a Scottish buyer of the goods.
[31] See G L Gretton, "Pledge, Bills of Lading, Trusts and Property Law" 1990 Juridical Review 23.

25.12 The wider notion of the property being returned to the provider for the purposes of sale while maintaining the pledge is viewed as advantageous practically because it is the provider who is likely to be better placed to sell than the creditor. A pledge of a bill of lading may also be a relatively short-term security.[32] Over forty years ago, however, the decision in *Poynter* was criticised by Dr Alan Rodger, later Lord Rodger of Earlsferry, as being contrary to principle by allowing the pledge to persist after the return of the goods.[33] In the Discussion Paper we raised the possibility of departing from the decision by asking if legislation should make it clear that the redelivery of pledged goods (or a pledged bill of lading) extinguishes the pledge. This would be without prejudice to any new system allowing for non-possessory security.

25.13 There was unqualified support for this proposal from several consultees, including Dr Ross Anderson, David Cabrelli, Chris Dun, Jim McLean and Dr Hamish Patrick. John MacLeod considered that this should only be done if a general codification of the law of pledge is undertaken. Other consultees, while stating that they agreed, said that any reform should not affect the right to proceeds under trust receipt financing. These included the Law Society of Scotland and Scott Wortley. As discussed above, the difficulty with such an approach is that it is simply not clear under the current law where the law of pledge stops and the law of trusts starts. We are also aware that trust receipt financing works in the same way in England and Wales as it currently does in Scotland. There would doubtless be resistance to Scotland-only reform here. We consider that the question should be reconsidered if and when there are relevant developments south of the border such as a major reform of secured transactions law.

113. The rule in *North-Western Bank Limited v Poynter, Son & Macdonalds,* that pledged property can be redelivered to the provider on the basis of a trust receipt without extinguishing the pledge, should not at the present time be abolished.

Enforcement of pledge under the Consumer Credit Act 1974

25.14 Sections 114 to 122 of the 1974 Act amount essentially to a code for enforcement of pledge where the person pledging the property is a consumer and the pledgee is a pawnbroker. The usual remedy of the pawnbroker is sale. No court order is required to authorise this. If that sale results in a surplus, that surplus must be returned to the (ex) debtor.[34] This is fair and reasonable and merely follows the general rule for rights in security.[35] There is, however, an exception. If the debt is a small one (currently up to £75)[36] enforcement is by forfeiture instead of sale. The pawnbroker becomes owner of the property. In the Discussion Paper[37] we showed that this was a strange and unfair rule. We gave the example of a painting being pawned for £70 and it later transpiring that it is worth £10,000. If the debtor defaults, the pawnbroker obtains a windfall. We concluded that as the 1974 Act currently stands there is no requirement to account to the pledger for the

[32] See Calnan, *Taking Security* para 2.49.
[33] A F Rodger, "Pledge of Bills of Lading" 1971 Juridical Review 193.
[34] Consumer Credit Act 1974 s 121.
[35] See eg Gretton and Steven, *Property, Trusts and Succession* para 21.24.
[36] 1974 Act s 120(1)(a).
[37] Discussion Paper, para 6.15.

£9,930 gain. The case of *Henderson v Wilson*[38] was decided on that basis (under predecessor legislation in similar terms).

25.15 We were also puzzled that there is no provision in the 1974 Act on reduction of the debt by the value of the article. For example, it is unclear when ownership of a £40 article is forfeited because a loan of £70 has not been repaid, whether the debt is now (a) zero; (b) £30; or (c) £70.[39]

25.16 Therefore we made two proposals. The first was that where, under the pawnbroking provisions of the Consumer Credit Act 1974, ownership of the pledged item is lost because the loan is below the prescribed figure (currently £75), the debt (if more than the value of the item) should be reduced by the value of the item. Secondly, we proposed that where, under the pawnbroking provisions of the 1974 Act, ownership of the pledged item is lost because the loan is below the prescribed figure, but the value of the item exceeds the loan, the loan should be discharged, and the pawnbroker should be obliged to pay the customer the surplus value (subject always to deduction of administrative expenses etc).

25.17 These proposals received strong support from consultees. Several, however, noted an issue of which we were indeed aware. The subject matter of the 1974 Act is reserved to the UK Parliament.[40] This means that we make no provision for this in our draft Bill. We consider also that reform is justified on a UK rather than Scotland-only basis. We therefore recommend:

114. (a) Where, under the pawnbroking provisions of the Consumer Credit Act 1974, ownership of the pledged item is lost because the loan is below the prescribed figure (currently £75), the debt (if more than the value of the item) should be reduced by the value of the item.

(b) Where, under the pawnbroking provisions of the Consumer Credit Act 1974, ownership of the pledged item is lost because the loan is below the prescribed figure (currently £75), but the value of the item exceeds the loan, the loan should be discharged, and the pawnbroker should be obliged to pay the customer the surplus value (subject always to deduction of administrative expenses etc).

Enforcement of pledge outwith the Consumer Credit Act 1974

Power of sale

25.18 Under the common law, which applies in non-consumer cases, the pledgee requires court permission to sell the pledged property on default.[41] It is, however, permissible for the pledge agreement to authorise a sale without the need for a court order.[42] This is known technically as *parata executie.*[43] But having a requirement to go to court where there is no

[38] (1834) 12 S 313.
[39] *McMillan v Conrad* (1914) 30 Sh Ct Rep 275, decided under predecessor legislation, suggests (a).
[40] Scotland Act 1998 Sch 5 Part II Head C7. See also para 1.39 above.
[41] See Steven, *Pledge and Lien* para 8-06.
[42] See eg *Moore v Gledden* (1869) 7 M 1016 at 1020 per Lord Neaves.
[43] See Steven, *Pledge and Lien* para 8-12. In South Africa the validity of *parata executie* clauses in terms of the right of access to the courts under the Constitution was successfully challenged in *Findevco (Pty) Ltd v Faceformat SA (Pty) Ltd* 2001 (1) SA 251 (E), but the Supreme Court subsequently departed from that

such agreement is perhaps odd in that the law seems more protective of the debtor in non-consumer cases than it is in consumer cases.[44] We noted in the Discussion Paper[45] that many European systems make a power of sale an implied term of a pledge. Given that application to the court increases enforcement costs and takes up court time, there is a case for reform here. It can, however, be argued that because an express clause is common in practice, there is no compelling need for reform.

25.19 We asked consultees whether the common law on a pledgee's power of sale is satisfactory and, if not, what changes are needed. Those who responded to this question all favoured an implied power of sale, but with different degrees of enthusiasm as to how necessary this was as a law reform exercise. Scott Wortley noted: "If experience is that the vast majority of people contract for an express power of sale I think the law should develop to reflect the practice to ensure that any unsophisticated creditors should have similar benefits."

Forfeiture

25.20 Forfeiture was discussed above in relation to the Consumer Credit Act 1974.[46] What is objectionable about forfeiture is that the value of the asset may be in excess of the debt. In contrast, allowing the secured creditor to appropriate the asset provided that payment of the excess value is made to the security provider is a different proposition and, increasingly, this has become competent under more recent legislation in other countries.[47] This is the approach taken in the DCFR,[48] where the provision makes it clear that the secured creditor can "appropriate encumbered assets only for the value of their recognised or agreed market price."

25.21 We asked consultees whether they agreed that, in cases outwith the Consumer Credit Act 1974, there should be a provision dealing with forfeiture clauses along the lines proposed in the DCFR. Consultees were generally supportive of such a provision.

Discussion

25.22 We have formed the view that there is much to be said for taking a broader approach to the reform of possessory pledge remedies. The reality is that the possessory pledge and the new statutory pledge serve the same purpose. They enable satisfaction of a debt to be made from moveable property. They merely differ in how they satisfy the publicity principle. The possessory pledge satisfies it by delivery. The new statutory pledge satisfies it by registration. We believe that the remedies available for the statutory pledge should also be available for the possessory pledge. This is the position under comparator legislation such as UCC–9 and the PPSAs. Thus the secured creditor should have an implied power of sale and alternative remedies such as leasing out the property or appropriation should also in principle be available. It is unclear under the current law whether lease is a remedy and it is

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conclusion in *Bock v Duburoro Investments* 2004 (2) SA 242 (SCA). For discussion, see A J M Steven, "Rights in Security" in E Reid and D Visser (eds), *Private Law and Human Rights: Bringing Home Rights in Scotland and South Africa* (2013) 418 at 423–428 and R Brits, *Real Security Law* (2016) 170–181.

[44] Although, pawnbrokers require to be licensed by the Financial Conduct Authority under the Financial Services and Markets Act 2000 ss 19 and 22, and Sch 2 para 23.

[45] Discussion Paper, para 15.9.

[46] See paras 25.14–25.17 above.

[47] Eg the French Civil Code art 2348 (as amended in 2006).

[48] DCFR IX.–7:105.

doubtful whether appropriation is possible.[49] We discuss the remedies in detail in Chapters 27 and 28 below. Of course, where property has been pledged by means of delivery there is no need to have rules on the taking of possession by the secured creditor, because that possession is already held. We recommend that:

115. Possessory pledge should have the same remedies as statutory pledge in non-Consumer Credit Act 1974 cases.

(Draft Bill, ss 67 to 84)

Codification

25.23 Finally, there is the question of whether the law of possessory pledge should be codified. This of course is the position in the European countries which have civil codes. It is also true in the UCC–9/PPSA jurisdictions because in effect there is a general code of security over moveable property in which pledge is included. In the Discussion Paper we expressed the view that the codification of the law of pledge would be less difficult than codification of the law of assignation.[50] The possibility of codification drew a mixed response from consultees. David Cabrelli, Jim McLean, John MacLeod, Professor Eric Dirix and Scott Wortley were in favour. The Faculty of Advocates and Dr Hamish Patrick were opponents, although gave no reason. Aberdeen Law School was also sceptical on the basis that the new statutory pledge would then be the primary option for creditors. Others, including Chris Dun and the Law Society of Scotland only saw a case for codification as part of a wider review and all, apart from Mr Dun, considered that such a review should include the Consumer Credit Act 1974. Brodies had no strong view.

25.24 We consider that a case for entire codification of pledge law at this time has not been made out. The relevance of the 1974 Act, the subject matter of which is reserved to the UK Parliament, would make this impossible to achieve in our draft Bill. There are also issues in the law of pledge which were not covered in the Discussion Paper and which would require consultation if we were to seek codification.[51] But, as a result of our recommendation above, the remedies for enforcement in non-consumer cases would become codified and this would be a considerable improvement on the current law. Of course codification could be revisited at a future date and this would certainly be the position if there were support for a UCC–9/PPSA approach in the UK. We recommend that:

116. The law of possessory pledge should not be codified at the present time.

[49] See Steven, *Pledge and Lien* paras 8-04 to 8-18 as to the remedies for pledge.
[50] Discussion Paper, para 15.12.
[51] Eg duties owed by the parties. See Steven, *Pledge and Lien* ch 7.

Chapter 26 Ranking of pledges

Introduction

26.1 In this chapter we deal with the issue of how pledges (both possessory and statutory pledges) rank with other rights in security and with diligence. Ranking, often also known as "priority",[1] is an important issue for rights in security.[2] The facilitation of access to finance by modern secured transactions laws depends on their ability to enable competing creditors to know clearly what their ranking is.[3]

26.2 The basic rule, that an earlier security has priority over a subsequent security, is straightforward. There is potential for complexity, however, particularly in multi-party situations. The phenomenon of the priority circle is well documented,[4] notably in the context of the floating charge. For reasons explained elsewhere,[5] our general approach in this Report is to leave the floating charge as it is and therefore solving such priority circles must await a future more general review of security rights and insolvency law.

General

26.3 Pledge is a true security right.[6] In other words, the secured creditor holds only a subordinate right in the encumbered property and the security provider retains ownership. Thus Anton could grant a statutory pledge over his car to Barry in respect of a loan from Barry. Under this arrangement, Anton is still owner of the vehicle. He could therefore grant a second statutory pledge over the same car to Catherine in respect of a separate loan from her. But in such circumstances, the question arises as to which security has priority. In other words, which security ranks first? This question is important because in the event of default the car may not be valuable enough to repay both loans.

26.4 Under the general law, ranking is by time of creation: *prior tempore potior jure* (prior in time stronger in right).[7] In property law terms, this means by time of real right. For statutory pledges this would normally mean the time of registration.[8] If Barry registers in the Register of Statutory Pledges on 1 November and Catherine on 2 November, Barry has the first ranking security and Catherine the second ranking security. Imagine that Anton defaults

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[1] Particularly in the UCC–9 and PPSA systems. See eg DCFR Book IX chapter 4.
[2] Thus eg in the UNCITRAL Legislative Guide on Secured Transactions, key objective (g) of an effective and efficient secured transactions law is "to establish clear and predictable priority rules".
[3] N O Akseli, *International Secured Transactions Law: Facilitation of Credit and International Conventions and Instruments* (2011) 225.
[4] A priority circle is where under ranking provisions creditor A ranks above creditor B, creditor B ranks above creditor C, but creditor C ranks above creditor A. See eg G Gilmore, *Security Interests in Personal Property* (1965) para 39.1; S Wortley, "Squaring the Circle: Revisiting the Receiver and 'Effectually Executed Diligence'" 2000 Juridical Review 325; and A MacPherson, "A Vicious Circle: the ranking of floating charges and fixed securities" 2014 Edinburgh Student Law Review 67. See also http://www.law.ed.ac.uk/research/making_a_difference/research_in_a_nutshell_the_ranking_problem.
[5] See Chapter 18 above and Chapter 38 below.
[6] See para 17.17 above.
[7] The rule is a familiar one in other jurisdictions. See eg Gullifer (ed), *Goode and Gullifer on Legal Problems of Credit and Security* para 5-26.
[8] See Chapter 23 above. Except in financial collateral cases where the security is created by possession or control. See Chapter 37 below.

and the car is sold for £5,000. Both loans are for £3,000. Barry would receive £3,000 and Catherine £2,000. Catherine would be left as an unsecured creditor for the remaining £1,000 of her loan.

26.5 In the Discussion Paper we asked consultees whether priority of the new security right to be introduced in respect of corporeal moveable property should be by date of registration.[9] There was strong support from consultees for this. There was similar support for our equivalent question in relation to incorporeal moveable property.[10] While our question was framed in terms of "date" it is more precise to refer to "time". As was seen in Chapter 6 above, modern security registers in other jurisdictions work on an electronic basis and record both the date and time of registration.

26.6 The time of registration would generally be the time of creation of a statutory pledge in respect of property owned by the provider. We deal with the issue of after-acquired property later in this chapter. We considered the issue of creation in relation to both current and after-acquired property in Chapter 23 above. That discussion is therefore of importance to the question of ranking too. In particular we concluded that a statutory pledge should be created at the time that the secured creditor obtains a real right and not back-dated to the time of registration. We recommended too that a statutory pledge should only be created when the relevant property became identifiable as encumbered property, perhaps by being identified in a schedule sent by the provider to the secured creditor. If a statutory pledge were to be set-up in this way it would be important for the parties to keep careful records.[11]

26.7 The general *prior tempore potior jure* rule would also govern the priority as between a statutory pledge and a possessory pledge. Imagine that Darcey grants a statutory pledge over her painting to Edna on 1 June. On 2 June Edna registers the security in the RSP. On 3 June Darcey agrees to pledge the painting to Frank. On 4 June Darcey delivers the painting to Frank. This means that he obtains a real right, as possessory pledge of course requires delivery.[12] But Edna's statutory pledge ranks above the possessory pledge, because she obtained her real right on 2 June.

26.8 A ranking issue is unlikely to arise between two possessory pledges. If a debtor has already pledged equipment to Bank A by handing it over to Bank A, the debtor cannot then hand over the equipment to Bank B to give it a pledge.[13] Where a possessory pledge is effected by constructive delivery the third party custodier, such as a warehouse, could be asked to hold the goods firstly for Bank A and then secondly for Bank B. But whether this would be effective is unclear. In view of the fact that the current law may limit pledge to actual delivery it is perhaps unsurprising that there does not appear to be authority on the question.[14]

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[9] Discussion Paper, para 16.55.
[10] Discussion Paper, para 18.28.
[11] As to the risk of fraudulent ante-dating it must be remembered that the earliest point from which a statutory pledge could rank is registration. Moreover, the secured creditor could have achieved a higher ranking by describing the encumbered property in the constitutive document as "all cars present and future" rather than "all cars to be identified in schedules". An alternative approach, which we considered, but rejected in the interests of commercial flexibility, would be to require the encumbered property to be described within the four corners of the constitutive document.
[12] See para 25.2 above.
[13] This is another reason why possessory pledge is restrictive.
[14] See para 25.2 above.

26.9 *Prior tempore potior jure* is of course a general rule. In the remainder of this chapter we make further recommendations as to which other rules this should be subject. Clearly, as a general rule, it should also be subject to any other enactment. For example, certain provisions in statutes relative to intellectual property require registration of rights in security in the relevant specialist register for there to be third party effect and thus for a statutory pledge over such property to rank.[15] Another example is the ranking rules for floating charges as regards any other right in security.[16]

26.10 We therefore recommend:

117. In general, the priority in ranking of any two pledges, or a pledge and a right in security other than a pledge, should be determined according to their creation, the earlier created having priority over the later.

(Draft Bill, s 64(1))

Future advances

26.11 Where security can cover future obligations, the following issue arises. Suppose that Suzanna grants to Tom an all-sums standard security over her house. At a time when the property is worth £1,000,000 and the loan from Tom is £700,000, Suzanna wants to borrow £100,000 from Ulrika, with Ulrika being granted a second-ranked standard security over the same property. Since there is £300,000 free "equity" in the property, it might seem that this deal is unproblematic.[17] But since the security held by Tom is an all-sums security, if Tom makes further advances to Suzanna in future, that would eat up the equity and undermine the value of Ulrika's security.

26.12 The same issue can arise with floating charges. Thus for both these types of security there is a rule whereby in this situation the priority of an earlier ranking security right can be frozen by means of a notice served on the holder of that security right.[18] In the Discussion Paper, we asked whether a similar rule would be appropriate for the new security (the statutory pledge).[19] We thought also that if the legislation were to be silent, then such a rule would probably be implied, on the basis that it is part of the common law of rights in security (though the point might be open to debate).[20] But we noted that there is no equivalent rule in UCC–9 and the PPSAs.[21] The question of course would not arise if the new security was incapable of securing future advances. But elsewhere in this Report we recommend, in line with the position for standard securities and floating charges, that it should be capable of doing so.[22]

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[15] See eg the Patents Act 1977 s 3 and the Trade Marks Act 1994 s 25(3)(a).
[16] Companies Act 1985 s 464.
[17] Though the contract between Suzanna and Tom might, and in practice commonly does, forbid Suzanna to grant any other security over the property without Tom's consent.
[18] Conveyancing and Feudal Reform (Scotland) Act 1970 s 13; Companies Act 1985 s 464(5).
[19] Discussion Paper, para 16.27.
[20] See in particular *National Bank of Scotland Ltd v Union Bank of Scotland Ltd* (1886) 14 R (HL) 1. (This case is sometimes cited with the defender's name, ie Union Bank, given first.)
[21] The PPSA rules allow "the first ranking creditor [to] erode the value of the subordinate creditor's security interest" and the only way to ensure this does not happen is for the second secured creditor to enter into a contractual priority arrangement with the first secured party. See Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* para 72.2.
[22] See paras 19.18–19.22 above.

26.13 Most consultees who responded to the question agreed that there should be a "freezing" provision for the new security. Chris Dun, however, dissented, writing: "This arrangement works poorly in practice in the context of standard securities and I would suggest should be avoided. In practice, it simply leads to expense in that there is a requirement for a ranking agreement to be entered into to maintain the "all sums" priority of the first ranking security – which in practice will invariably prohibit the grant of postponed security." We think that Mr Dun's point has much force. We are also struck by the fact that there is no "freezing" provision in UCC–9 and the PPSAs.

26.14 On reflection, we think that if there were to be such a provision secured creditors would invariably seek to exclude it by means of a "negative pledge" clause. Such clauses are typically found in floating charges and forbid the grant of further security rights. They are to be found in the legislation on floating charges and they make that legislation more complicated.[23] But without such a rule negative pledge clauses would not be required for that purpose because an earlier created statutory pledge would always rank above a subsequent statutory pledge unless there was a ranking agreement to the contrary.[24] We think that the same rule should apply to possessory pledges. We accordingly recommend:

118. The priority in ranking of a pledge should be the same irrespective of whether the secured obligation is an obligation owed or is an obligation which will or may become owed.

(Draft Bill, s 64(5))

After-acquired property

26.15 The general *prior tempore potior jure* rule requires to be carefully considered in relation to property which the provider has acquired after the grant of the statutory pledge. Earlier we recommended that a statutory pledge should be created on the secured creditor obtaining a real right in the asset, which in respect of after-acquired property means that this cannot happen until the provider has become owner.[25] We argued that this was preferable to back-dating the priority artificially to the time of registration. For possessory pledge, the need to deliver the assets means that the security is generally restricted to property which the provider currently owns and is thus able to deliver.[26]

26.16 As we did in the Discussion Paper, we think that it is helpful to consider policy by reference to examples.[27] Imagine that Horace grants a statutory pledge in favour of Isabel over his present and future pianos. It is registered in the RSP on 1 June 2020. At that time Horace has one piano. Isabel duly acquires a real right in the piano. On 1 December 2022 Horace buys a second piano from John. Clearly Isabel did not acquire a real right in that piano two years previously on registration. At that point the piano did not belong to Horace.

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[23] Under the Companies Act 1985 s 464(1) and (1A) a floating charge with a negative pledge clause will rank above a subsequent fixed security. The Bankruptcy and Diligence etc. (Scotland) Act 2007 Part 2 takes a more simple approach of floating charges generally ranking above subsequent fixed securities, although it still has a "freezing provision". See 2007 Act s 40(5).

[24] On ranking agreements, see para 26.35–26.39 below.

[25] See paras 23.22–23.27 above. The property would also require to be identifiable as encumbered property.

[26] But cf para 25.3 above where we recommend that if the property is not the provider's at the time of delivery, but subsequently becomes the provider's the pledge would be created at that point. We doubt that this situation would be usual.

[27] Discussion Paper, paras 16.50–16.55.

Indeed it might not yet even have been manufactured. Isabel can only acquire her real right on Horace becoming owner.

26.17 This rule also has the following consequence. Imagine that John had granted a statutory pledge over his piano in favour of Quentin, which was registered in the RSP on 1 June 2021. When John subsequently transferred the piano to Horace on 1 December 2022, he did so without Quentin's permission. Therefore Quentin's statutory pledge subsists.[28] To say that Isabel's statutory pledge would rank above Quentin's security because it was registered a year earlier (on 1 June 2020) would be wrong. The piano was encumbered by Quentin's security before it ever entered into Horace's patrimony.

26.18 Let us develop the example further. As well as granting the statutory pledge in favour of Isabel registered on 1 June 2020, he grants a similar statutory pledge over his present and future pianos in favour of Jacqueline. This statutory pledge is registered on 1 May 2021. On 1 December 2022 Horace buys the second piano. Both Isabel and Jacqueline would acquire their real right in security at the same moment. In the Discussion Paper, we said that in such a situation Isabel's security right would nevertheless rank first and that this was a "twist" in the law of ranking.[29]

26.19 We noted that under UCC–9 and the PPSAs, as well as the DCFR, a security right is deemed to be perfected at the time of registration, even although in respect of after-acquired assets the right cannot be created until the asset is acquired.[30] We criticised this on the basis that it is undesirable for a juridical act to have retroactive effect. For after-acquired assets, the real right should be obtained on acquisition of the property by the provider.[31] We consider nevertheless that the "twist" mentioned in the previous paragraph should be provided for in the new legislation to make it clear that in the situation described Isabel's statutory pledge would rank first. In other words, ranking would be by date and time of registration.[32]

26.20 We therefore recommend:

119. Where a provider grants two or more statutory pledges over property which, as at the time the pledges are granted, is not the provider's, the priority in ranking of any two of the pledges should be determined according to the dates on which they are registered, the earlier having priority over the later.

(Draft Bill, s 64(2) & (3))

[28] Assuming that it was not a low-value piano and the good faith acquisition rule which we recommended in Chapter 24 did not apply.
[29] Discussion Paper, para 16.53.
[30] Discussion Paper, para 16.52. See eg DCFR IX.–3:305(2) and 4:101(2)(a).
[31] Subject to an exception in respect of property acquired after the commencement of insolvency. See paras 23.28–23.32 above.
[32] Normally, this would mean the date and time of registration of the constitutive document, but if the pledge over the particular property was only granted by means of an amendment document it would be the date and time of its registration which would matter.

Ranking with floating charges

26.21 The ranking of floating charges is regulated by section 464 of the Companies Act 1985.[33] We consider that a statutory pledge created before a floating charge has attached should rank above the floating charge. This is in line with the existing rule found in section 464(4)(a): "a fixed security, the right to which has been constituted as a real right before a floating charge has attached to all or any part of the property of the company, has priority of ranking over the floating charge". A statutory pledge would be created in particular assets when the secured creditor obtains a real right in these. Thus for after-acquired assets the real right would only be obtained when the provider becomes owner[34] and therefore the statutory pledge holder would not be preferred to the floating charge holder as regards assets acquired post-attachment.

26.22 We think that it would be helpful to amend the 1985 Act to make it clear that the statutory pledge is to be regarded as a "fixed security" for the purposes of the ranking rules in that Act. A similar amendment should be made to the Insolvency Act 1986.

26.23 We therefore recommend:

120. The definitions of "fixed security" in section 486(1) of the Companies Act 1985 and section 70(1) of the Insolvency Act 1986 should be amended to include a statutory pledge.

(Draft Bill, s 65)

Ranking with ship mortgages

26.24 Earlier in this Report we recommend that a statutory pledge should not be competent in respect of vessels over which it is competent to grant a ship mortgage.[35] This is to avoid undue proliferation of security types. The situation, however, is not entirely straightforward. Ship mortgages are only possible where a ship is registered in certain parts of the UK Ship Register.[36] As the WS Society noted in its response to the Discussion Paper, any UK ship can in principle be registered in Part 1 of the Register and therefore be the possible subject of a ship mortgage.

26.25 Hence the following situation, although probably unlikely in practice, could occur. An unregistered ship, perhaps a yacht, could have a statutory pledge granted over it. The owner might then subsequently register the yacht in Part 1 of the UK Ship Register and grant a ship mortgage. Here the usual ranking rule that the earlier-created security should rank first would apply.[37]

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[33] The provisions are applied to limited liability partnerships by the Limited Liability Partnerships (Scotland) Regulations 2001 (SSI 2001/128) reg 3 and Sch 1; European Economic Interest Groupings by the European Economic Interest Grouping Regulations (SI 1989/638) reg 18 and Sch 4; co-operative and community benefit societies by the Co-operative and Community Benefit Societies Act 2014 s 62 and building societies by the Financial Services (Banking Reform Act) 2013 Commencement (No. 8 and Consequential Provisions) Order 2015 (SI 2015/428) art 4.

[34] See paras 23.22–23.27 and 26.14–26.19 above.

[35] See paras 21.7–21.11 above.

[36] See para 21.11 above.

[37] See para 26.4 above.

Ranking with aircraft mortgages

26.26 Elsewhere in this Report we recommend that a statutory pledge should not be competent in respect of aircraft where an aircraft mortgage or international interest under the Cape Town Convention can be granted.[38] In the unlikely event that a statutory pledge were granted over assets which subsequently became subject to one of those types of security,[39] the relevant legislation has ranking rules which regulate the matter.[40]

Ranking with tacit security rights

26.27 Certain security rights arise by operation of law rather than being granted. The leading examples are lien and the landlord's hypothec. The former allows someone to retain an article until a bill is paid. For example, a repairer may assert a lien for work done.[41] The landlord's hypothec allows the landlord in a commercial lease to seize the tenant's goods for rent arrears.[42] In the Discussion Paper,[43] we noted that floating charges rank behind "any fixed security arising by operation of law".[44] We said also that UCC–9 and the PPSAs had provisions under which tacit securities prevail over express securities.[45]

26.28 We asked consultees two separate questions. The first was whether they agreed that any new security right should be without prejudice to the landlord's hypothec. The second was whether the new moveable security should be postponed, in terms of ranking, to security rights arising by operation of law. Perhaps unsurprisingly given that the landlord's hypothec is a security arising by operation of law consultees generally took a consistent approach here. Most of those who responded were of the view that tacit securities should have prior ranking. We agree that this should be the policy for the statutory pledge. But some also called for clarification of the general law relating to the landlord's hypothec, where there is some uncertainty following statutory reform in 2007.[46] Dr Hamish Patrick favoured abolition of the hypothec. Such matters must, however, be left for the future.

26.29 It is perhaps less likely that there will be a competition between a tacit security and a possessory pledge because of the need for the secured creditor to have possession. Thus if a business has handed over equipment to a bank, the business's landlord will not be able to use its hypothec in relation to the equipment as it will not be in the leased premises.[47] But in some cases there could be a competition. For example, goods in a warehouse might be pledged to a bank by means of constructive delivery (intimation to the warehouse) but the warehouse has a lien over them in respect of its charges.[48] We consider here that the lien should have priority.

26.30 We recommend that for both possessory and statutory pledges:

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[38] See paras 21.12 and 21.16–21.20 above.
[39] Perhaps engines which were adapted to become aircraft engines to which the Cape Town Convention applies.
[40] Mortgaging of Aircraft Order 1972 (SI 1972/1268) art 14; International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015 (SI 2015/912) reg 16.
[41] For example, *Tyne Dock Engineering Co Ltd v Royal Bank of Scotland Ltd* 1974 SLT 57.
[42] Bankruptcy and Diligence etc. (Scotland) Act 2007 s 208. This right in security originated in Roman law.
[43] Discussion Paper, para 16.58.
[44] Companies Act 1985 s 464(2).
[45] UCC § 9–333; NZ PPSA 1999 s 92.
[46] See A McAllister, "The Landlord's Hypothec: Down but is it out?" 2010 Juridical Review 65; A J M Steven and S Skea, "The landlord's hypothec: difficulties in practice" 2010 SLT (News) 120.
[47] The landlord's hypothec affects goods in the leased subjects.
[48] See eg *Laurie & Co v Denny's Tr* (1853) 15 D 404.

121. Where property is subject both to a pledge and to a security arising by operation of law, the security arising by operation of law should have priority over the pledge.

(Draft Bill, s 64(4))

Interaction with diligence

26.31 The statutory pledge would interact with diligence under the general law, as do possessory pledges at the present time. Once again the general rule is *prior tempore potior jure.* We consider that the law would be made more accessible here by restating it in statute.

26.32 For example, Kirsten is a sole trader who owns equipment. On 1 June she grants a statutory pledge over it to the Lothian Bank which is immediately registered in the RSP. On 15 June, Mike, a creditor of Kirsten, attaches the equipment. The attachment would be effective but would rank after the pledge. Conversely, if Mike had attached the equipment on 31 May the pledge would be effective when it was created on 1 June but it would rank after the diligence.

26.33 Consideration needs to be given to the situation where further advances are made in relation to an obligation secured by a pledge. For example, the pledge granted by Kirsten to the Lothian Bank is for all sums owed by Kirsten to the bank. The pledge is registered. Kirsten is immediately lent £10,000 by the bank. One month later Mike attaches the equipment. Three days later the bank lends Kirsten a further £5,000. Here we consider that the bank's priority should generally be limited to the £10,000 advanced before Mike attached the equipment. If, however, the bank is contractually obliged, or has undertaken, to lend the further £5,000 prior to Mike attaching then in that event it should have priority for the entire £15,000. This rule reflects the position in relation to standard securities where a further advance is made by a first ranking security holder who has received notice of a subsequent standard security,[49] as well as the better view of the ranking of inhibiting creditors as against standard security holders making further advances.[50] Secured creditors considering making further advances can protect themselves by ascertaining whether any diligence has been carried out prior to making the advance.

26.34 We recommend:

122. (a) Where diligence is executed in respect of property all or any part of which is encumbered by a pledge, the pledge has priority of ranking over the diligence, except as regards further advances made after the execution of the diligence which are not required to be made by a contractual agreement entered into or undertaking given before such execution.

[49] Conveyancing and Feudal Reform (Scotland) Act 1970 s 13.
[50] G L Gretton, *The Law of Inhibition and Adjudication* (2nd edn, 1996) 150–154.

(b) Where a pledge is created over property in respect of all or any part of which diligence has been executed, the diligence has priority in ranking over the pledge.

(Draft Bill, s 66)

Ranking agreements

26.35 We consider again in line with the general law that it should be possible for a secured creditor holding a pledge to enter into a ranking agreement[51] with the holder of another pledge, or indeed another security right such as a floating charge. We think that such an agreement should be in writing for evidential reasons.

26.36 The agreement should not affect third parties who have not consented to it.[52] Thus imagine that there are three statutory pledges over the same asset in favour of Alan, Ben and Carol. Alan's security ranks first, then Ben's and then Carol's. Alan and Carol agree that Carol should rank before Alan. Unless Ben consents to the arrangement, Ben's priority should be unaffected.[53]

26.37 On the other hand we think that a ranking agreement should bind the successors of the original parties. Where Alan has entered into a ranking agreement with Carol whereby Alan's statutory pledge ranks behind Carol's, Alan should not be able to defeat that by assigning his statutory pledge to David. Here David should also be bound by the agreement unless Carol agrees otherwise.

26.38 On the basis that ranking agreements should be personal to the parties and their successors we consider that ranking agreements in respect of statutory pledges should not be registrable in the RSP.[54]

26.39 We recommend:

123. (a) The secured creditor and the holder of another pledge or other right in security should be able to set out in writing an agreement as to ranking.

(b) Such an agreement should have effect only as between the parties to the agreement and their successors and should not be registrable.

(Draft Bill, s 64(6) & (7))

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[51] Sometimes known as a "subordination agreement".

[52] In England, see *Re Woodroffe's (Musical Instruments) Ltd* [1986] Ch 366. But cf *Re Portbase Clothing Ltd* [1993] Ch 388. For discussion, see Gullifer (ed), *Goode and Gullifer on Legal Problems of Credit and Security* para 5.62.

[53] In practice this may mean Alan continuing to enforce as Alan ranks above Ben. Alan would then pay over Alan's share (or other agreed amount) to Carol.

[54] Under the Companies Act 2006 s 859O(1)(b) it is possible but not mandatory to register a ranking agreement affecting a charge (security right) granted by a company, in the Companies Register. This only became possible in 2013 and it has been doubted whether the power to register will be exercised frequently. See Calnan, *Taking Security* paras 6.113–6.114.

Chapter 27 Enforcement of pledge (1)

Introduction

27.1 Where the debtor defaults on the secured obligation, the secured creditor will normally wish to recover what is due to it by enforcing the security right. This is the reason for taking the security right in the first place.[1] The secured creditor is able to proceed against the encumbered property rather than simply having to rely on its rights under the debt contract. Such contractual rights are of little avail if the debtor has become insolvent or indeed has disappeared without leaving a forwarding address.

27.2 In the Discussion Paper we expressed the view that, so far as possible, enforcement of the new security right should be swift and inexpensive.[2] The longer it takes to enforce a security right and the more expensive that process is, the less effectively the security right works.[3] Debtors themselves consequently suffer because delays in enforcement tend to result in more accumulated interest and the expenses of the process will usually fall on the debtor too.

27.3 Nevertheless, there need to be appropriate rules protecting debtors. The enforcement of the security right will mean that assets of the debtor[4] will be used to recover the secured debt. Protection is particularly required in a consumer context. But it should also be remembered that we have already recommended safeguards by limiting the extent to which the security can be granted over non-business assets.[5] In addition the protections in the Consumer Credit Act 1974, in relation to any grant of a security right by a consumer, would also apply.[6] We say more about these later.[7]

27.4 We discussed enforcement only briefly in the Discussion Paper on the basis that for the most part enforcement involves issues of technique rather than questions of fundamental policy. We noted that there were several models for enforcement that could be consulted. These include UCC–9, the PPSAs, the DCFR, the EBRD Model Law and the Murray Report,[8] as well as existing schemes in Scotland, such as the rules for enforcing standard securities contained in the Conveyancing and Feudal Reform (Scotland) Act 1970.[9] We have drawn on these in the preparation of this Report. We have found the DCFR particularly helpful.

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[1] See para 1.3 above.
[2] Discussion Paper, para 16.63. Thus for example one of the key objectives of the UNCITRAL Legislative Guide on Secured Transactions is "to facilitate efficient enforcement of a secured creditor's rights". See https://www.uncitral.org/pdf/english/texts/security-lg/e/09-82670_Ebook-Guide_09-04-10English.pdf at p 21.
[3] See eg Calnan, *Taking Security* para 1.29.
[4] Assuming, as is usually the case, that the debtor and the provider are the same person.
[5] See paras 19.36–19.55 above.
[6] See in particular Consumer Credit Act 1974 Parts 7, 8 and 9. See W C H Ervine, *Consumer Law in Scotland* (5th edn, 2015) paras 8-134 to 8-153.
[7] See paras 27.14–27.26.
[8] And now too the UNCITRAL Model Law on Secured Transactions of 2016.
[9] Although, in relation to the 1970 Act, we were aware of the deficiencies in the current rules and the fact that this area will be reviewed as part of our forthcoming project on heritable securities. See Scottish Law Commission, Ninth Programme of Law Reform (Scot Law Com No 242, 2015) para 2.17.

27.5 In this chapter and the next one we set out the enforcement rules which we think should apply to pledges under the new statutory scheme. This chapter considers the circumstances in which a pledge can be enforced, when a court order should be required and, in the case of the statutory pledge, how possession of the encumbered property can be obtained. Chapter 28 focusses principally on realisation of the encumbered property and distribution of the proceeds.

Consultation: general

27.6 In the Discussion Paper we asked two broad questions on enforcement of the new security right (the statutory pledge). The first asked consultees for their views in general terms, but this question was located in the chapter on reform of security over corporeal moveable property.[10] The other question asked for views on enforcement in so far as the collateral consisted of personal rights.[11] But as discussed in Chapter 22 above we recommend at least initially that these should not be the subject of a statutory pledge.

27.7 Generally, the questions unsurprisingly drew broad responses from consultees. Dr Ross Anderson agreed "that enforcement should be as easy as possible". ABFA argued that enforcement procedures "should be kept simple". Aberdeen Law School said that: "it seems desirable that recourse to the courts is not necessary in all instances". ICAS/R3 commented that "[t]he methodology of enforcement has to be given careful consideration". We agree.

27.8 In Chapter 25 we considered the questions in the Discussion Paper on the enforcement of possessory pledges.[12] We say more about this below.

Consultation: statutory pledges and receivership

27.9 The Discussion Paper also considered the specific issue of whether the statutory pledge should be enforceable (if so desired by the creditor) by a form of receivership.[13] This type of enforcement mechanism for security rights is recognised under English law but has also been made available in Scotland for enforcement of floating charges.[14] In England and Wales the type of receiver appointed by a floating charge holder under the Insolvency Act 1986 is known as an "administrative receiver".[15] In addition there are so-called "LPA receivers" who can be appointed under mortgages or charges to receive the income from the encumbered property (typically rents).[16]

27.10 We expressed doubt about statutory pledges being enforceable by receivership. We noted that if the debtor became insolvent, the security right would be enforceable through liquidation or administration or alternatively, sequestration because the general law of insolvency gives security rights their due ranking. Outwith insolvency, a creditor could appoint an agent to act, a matter to which we return below.[17] We noted also that

[10] Discussion Paper, para 16.71.
[11] Discussion Paper, para 18.32.
[12] See paras 25.18–25.22 above.
[13] Discussion Paper, para 16.70.
[14] Originally by the Companies (Floating Charges and Receivership) (Scotland) Act 1972. See now the Insolvency Act 1986 ss 50–71. See generally J H Greene and I M Fletcher, *The Law and Practice of Receivership in Scotland* (3rd edn, by I M Fletcher and R Roxburgh, 2005).
[15] Insolvency Act 1986 s 29(2).
[16] The "LPA" comes from the authorising statute: Law of Property Act 1925 s 101.
[17] See paras 27.29–27.31 below.

receivership is a problematic concept, under which the receiver is nominally the debtor's agent, when in substance he or she is really acting for the creditor.[18] And when a receiver is appointed by a floating charge holder, the receivership goes beyond a mere mechanism for enforcing security. There is, for example, the power to hire and dismiss employees.[19] Receivership is therefore to some extent a concept of insolvency law. The Enterprise Act 2002 now greatly limits the extent to which it is available for enforcement of floating charges.[20]

27.11 Consultees who commented on the issue generally agreed that receivership should not be used to enforce the statutory pledge. This was the unqualified view of the Judges of the Court of Session. Brodies noted that the security would potentially be over a more limited class of assets than the floating charge and that Scotland has not, to date, followed the English position of allowing receivers to enforce fixed securities. They therefore agreed that the extension of enforcement through receivership should not be followed. Instead they suggested "a direct power of sale and additional or ancillary powers of enforcement" to be held by the holder of the statutory pledge. The Law Society of Scotland agreed. Scott Wortley stated: "Receivership is to me an unsophisticated tool which targets the management of the business and has knock on consequences for third party creditors as actions are carried out for the benefit of one creditor. The powers of the receiver are substantial. I think they extend beyond what is required in this case."

27.12 We therefore recommend:

124. The statutory pledge should not be enforceable by receivership.

A unitary approach to the enforcement of possessory pledges and statutory pledges

27.13 In Chapter 25 above we recommended that (a) possessory pledges not regulated by the Consumer Credit Act 1974, and (b) statutory pledges, should in principle have the same enforcement regime. This was because a possessory pledge and the new statutory pledge both serve the same purpose of enabling satisfaction of a debt to be made from assets. They simply differ in how they satisfy the publicity principle: the possessory pledge by delivery and the statutory pledge by registration. There require to be some minor differences in relation to enforcement. In particular for statutory pledges there needs to be a mechanism to take direct possession of the property. A unitary scheme for enforcement of security rights over moveable property is a feature of legislation in other countries, notably under UCC–9 and the PPSAs.

Consumer Credit Act 1974

Introduction

27.14 The Consumer Credit Act 1974 is one of the more complex pieces of legislation currently on the statute book. As we noted in Chapter 1, legislative competence to amend it

[18] See Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 18.61.
[19] Insolvency Act 1986 Sch 2 para 11.
[20] It amended the Insolvency Act 1986 inserting new sections 72A–72H.

is reserved to the UK Parliament.[21] This means that our draft Bill, which is intended for implementation by the Scottish Parliament, requires to work within the terms of the 1974 Act.

General application

27.15 The provisions in the 1974 Act which regulate security rights granted by "consumers" within the meaning of the Act would automatically apply to the new statutory pledge.[22] The 1974 Act has provisions which apply more generally to consumer credit agreements which it regulates. In particular a default notice must be served on the debtor at least 14 days before any enforcement steps can be taken.[23]

27.16 We noted in Chapter 19 above that the 1974 Act uses the term "individual" to refer to consumers. That term is defined more widely than might be expected as including:

> "(a) a partnership consisting of two or three persons not all of whom are bodies corporate; and
>
> (b) an unincorporated body of persons which does not consist entirely of bodies corporate and is not a partnership."[24]

But certain credit agreements made with individuals are outwith the scope of the 1974 Act, notably loans of more than £25,000 taken out for business purposes and loans of more than £60,260 to "high net worth individuals".[25]

Pawn

27.17 The 1974 Act has an enforcement scheme for possessory pledges which are subject to it, in other words pawns[26] by individuals, small partnerships involving individuals and unincorporated bodies involving individuals. It follows that when the 1974 Act enforcement scheme is applicable our recommended scheme could not be applicable. This means that our scheme in relation to possessory pledges would be principally applicable where the provider of the statutory pledge is a company or LLP. We recommend:

> **125. In the scheme for the enforcement of pledges, the expression "pledge" should not include a pledge as defined in section 189(1) of the Consumer Credit Act 1974.**
>
> (Draft Bill, s 67)

Applicability of other protections

27.18 In the Discussion Paper we asked consultees if a new non-possessory security over corporeal moveable property were introduced, whether the pro-consumer protections in the Consumer Credit Act 1974 should be amended so as to extend to it (other than those

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[21] See paras 1.39–1.42 above.
[22] See, for example, the Consumer Credit Act 1974 ss 105–113.
[23] Consumer Credit Act 1974 ss 87–89.
[24] Consumer Credit Act 1974 s 189(1). For discussion, see W C H Ervine, *Consumer Law in Scotland* (5th edn, 2015) para 8-35.
[25] See para 19.52 above.
[26] The historic inter-relationship between the words "pledge" and "pawn" is unclear but the latter seems to mean a pledge in favour of a pawnbroker or professional-pledge taker. See Steven, *Pledge and Lien* paras 2-15 to 2-16.

protections that would apply automatically).[27] But we did not elaborate which non-automatically applicable protections we particularly had in mind.

27.19 Consultees were generally supportive, although their answers tended to be non-specific. Dr Ross Anderson wondered if we meant amending the definition of "security" in section 189 of the 1974 Act. But the current definition seems wide enough to include the new statutory pledge.[28]

27.20 The Law Society of Scotland and several law firm consultees all suggested that the new security right should have similar protections to hire-purchase. To put it another way, the statutory pledge should not be seen by creditors as a mechanism to evade the protections of hire-purchase law.

27.21 There is, however, a fundamental conceptual difference between hire-purchase and the statutory pledge. The former is a contract to hire goods with an option to purchase. It is necessarily restricted to acquisition finance. The latter is the grant of a security right by a person over that person's property.[29] It is not limited to acquisition finance. Nevertheless, functionally the two can appear very similar.

27.22 We have considered the protections conferred on hire-purchasers in various parts of the 1974 Act. In our view, three are of particular significance.[30] It is worth, however, making a preliminary point. As a result of our earlier recommendation that the statutory pledge should only be available for consumer finance transactions where the property is above a certain value, the statutory pledge would be available for a narrower category of assets than hire-purchase.[31]

27.23 The first protection is that where the creditor wants to take possession of the property because the hirer is in default, a court order is required if the creditor requires to enter any premises to do so.[32] We agree with this approach. Our recommendation below generally requiring a court order to enforce where the provider is an individual acting outwith the course of a business covers this situation.[33]

27.24 The second protection can be referred to as the "one third" rule. Where the hirer has paid one third of the purchase price the creditor has to apply for a court order to be allowed to recover the goods.[34] The apparent policy here is to differentiate hirers who cannot pay and hirers who will not pay, because where a debtor has repaid less than one third of debt a court is likely to grant an enforcement order rather than allow any relief which the 1974 Act offers.[35] We set out below our recommendations as to the circumstances in which a court

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[27] Discussion Paper, para 16.78.
[28] The definition refers to "a mortgage, charge, pledge, bond, debenture, indemnity, guarantee, bill, note *or other right provided by the debtor* or hirer, or at his request (express or implied), *to secure the carrying out of the obligations of the debtor* or hirer under the agreement" (our emphasis).
[29] Although this could include future property.
[30] These typically apply to conditional sale as well as hire-purchase.
[31] See paras 19.36–19.51 above.
[32] Consumer Credit Act 1974 s 92. Goods will almost always be within premises. An exception would be a motor vehicle on the street.
[33] See paras 27.46–27.54 below.
[34] Consumer Credit Act 1974 s 90.
[35] Law Commission, Bills of Sale (Law Com No 369, 2016) paras 7.72 and 7.77.

order should be required before enforcement can take place,[36] but we are not persuaded that they should be tied to cases where a certain amount of the secured debt has been repaid.

27.25 The third protection is known as the "one half" rule. Where the hirer has paid half the purchase price, he or she is entitled to return the property and have no further personal liability.[37] In other words, the remaining debt is cancelled. This is controversial in the case of motor vehicles because the speed at which new cars depreciate means that the finance company can suffer a loss as a result of it. Under the Consumer Credit Trade Association Code, which operates in relation to bills of sale and motor vehicles in England and Wales, the rule is a broader one. The borrower is entitled to surrender the motor vehicle to the lender and be discharged of personal liability at any time prior to repossession agents being instructed even if no repayments have been made.[38] The Law Commission for England and Wales has recommended that this wider rule becomes the law in relation to its proposed new "goods mortgage".[39]

27.26 For our part, we consider that conceptually such a rule sits more easily with the situation where the creditor has ownership of the asset. This is certainly the position for hire-purchase and bills of sale, but for the new goods mortgage the creditor would not acquire ownership.[40] With the statutory pledge the provider has ownership. We are therefore not persuaded that the "one half" rule is appropriate for statutory pledges. Moreover, it is essentially a rule about personal liability for a debt being cancelled, which is in principle outwith the scope of this Report. In some cases it may also disadvantage the provider because the asset is worth more than the remaining debt. Nevertheless, if the statutory pledge was deliberately used to defeat the operation of the "one half" rule applicable in hire-purchase the position would clearly need to be reviewed, notwithstanding the conceptual difficulties and the fact that the subject matter of the Consumer Credit Act 1974 is reserved to the UK Parliament.

Only prescribed remedies

27.27 We consider that the secured creditor should be limited to the remedies set out in statute for the enforcement of a pledge. This provides certainty, as well as protecting the provider of the statutory pledge (normally the debtor). We recommend:

> **126. A pledge should be enforceable in no other way than in accordance with the remedies set out in statute.**
>
> (Draft Bill, s 68(1))

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[36] See paras 27.46–27.54 below.
[37] Consumer Credit Act 1974 ss 99 and 100.
[38] Law Com No 369, 2016 para 7.106. Bills of sale tend to be granted over older vehicles where depreciation is less of an issue.
[39] Law Com No 369 paras 7.108–7.112.
[40] Law Com No 369 para 4.42 recommended that "a goods mortgage should continue to take effect by transferring ownership to the lender unless the parties agree that it should take effect as a charge". But in its *Replacing bills of sale: a new Goods Mortgages Bill, Consultation on draft clauses* (2017) Appendix 2 the Law Commission announced a change in policy and proposed that the goods mortgage should be a type of charge. The main reasons given are set out in para 2.5 of that Appendix and include the fact that transfers of ownership by way of security have mainly become obsolete.

Enforcement: when?

27.28 The circumstances in which a pledge can be enforced should be set out. We consider that there should be two.[41] The first is where there is failure to perform the secured obligation. Thus if the security right secures repayment of a loan by B Ltd to a bank which is due on 1 April and B Ltd fails to pay on that date the bank should be entitled to enforce, subject to any agreement between the parties on the matter. The second is in such other circumstances as are agreed between the provider and the secured creditor. For example, the secured creditor may wish to stipulate that the security becomes enforceable immediately on the appointment of a trustee in sequestration or liquidator. We think that an agreement between the provider and secured creditor as to the relevant circumstances should require to be in writing. We recommend:

127. (a) A statutory pledge should be enforceable:

(i) where there is failure to perform the secured obligation, or

(ii) in such other circumstances, if any, as are agreed between the provider and the secured creditor.

(b) Any such agreement should require to be set out in writing.

(Draft Bill, s 68(2) & (3))

Enforcement: by whom?

27.29 We concluded above that it would not be appropriate for enforcement to proceed by way of receivership.[42] Nevertheless, the secured creditor rather than acting directly may wish to appoint an agent to enforce the pledge. For example, insolvency practitioners and law firms are commonly involved in enforcement of security rights. In principle we think that it should be possible for the secured creditor to enforce through the agency of others.

27.30 A number of our consultees expressly supported this approach. One law firm[43] commented: "We suggest that the best solution is to confer powers on the security holder but give the security holder express statutory power to appoint agents to act on its behalf and entitled to exercise all the relevant powers etc."

27.31 Floating charges are enforced by insolvency practitioners but enforcement involves taking over the running of the company or other corporate body. In contrast a pledge (possessory or statutory) will be over a more limited class of assets, so requiring an insolvency practitioner always to act seems unnecessary. In relation, however, to taking possession of encumbered property, we consider that for protective reasons only prescribed categories of person should be able to act for the secured creditor. We discuss this below.[44] In general we recommend:

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[41] This follows the definition of default in the DCFR IX.–1:201(5).
[42] See paras 27.9–27.12 above.
[43] Dundas & Wilson.
[44] See paras 27.64–27.81 below.

128. A statutory pledge should be enforceable by or on behalf of the secured creditor.

(Draft Bill, ss 68 and 118(4))

Duties of secured creditor

27.32 In order to protect the provider it is necessary to make the secured creditor subject to certain duties. Comparator legislation in numerous other jurisdictions places a duty on the secured creditor to act in accordance with reasonable standards of commercial practice.[45] Thus, for example, there should be no harassment of the provider, or action or non-action by the secured creditor which leads to the devaluation of the encumbered property.[46] Such a duty is sometimes imposed on the secured creditor generally, or specifically in relation to enforcement, the latter being the approach of the DCFR. There is a difference between our recommended legislation and most comparators in that our approach is less codal. Enforcement of pledges would be subject to the general law, such as the rules on catholic and secondary security rights,[47] like enforcement of existing security rights.[48] It may be that the common law would impose a duty to act in accordance with reasonable standards of commercial practice. But, as the position is not certain, we consider that there would be value in having a statutory rule in relation to enforcement. Given that so many other jurisdictions have a similar rule, indeed wider where not limited to enforcement, we are not persuaded by the submission made by R3 to our draft Bill consultation of July 2017 that this would be "a rogue's charter to resist and challenge as invalid any enforcement on the allegation of a failure to follow an unspecified standard practice."

27.33 We accordingly adopt the approach of the DCFR. The result would be that where a security provider or other party with an interest[49] could show that the duty was (set to be) breached usual court remedies such as interdict and damages would be available.

27.34 Some comparator legislation also places a duty on the secured creditor to act in good faith.[50] The role of good faith in Scottish private law is controversial,[51] not least in relation to rights in security.[52] We are therefore not persuaded of the case to have it as an express statutory requirement in this case.[53]

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[45] For example, Saskatchewan PPSA 1993 s 65(3); NZ PPSA 1999 s 25(1); Australian PPSA 2009 s 111; Malawi PPSA 2013 s 5(1); DCFR IX.–7:103(4) and UNCITRAL Model Law on Secured Transactions art 4.

[46] See Drobnig and Böger, *Proprietary Security in Movable Assets* 717.

[47] Gloag and Irvine, *Law of Rights in Security* 58–65. In essence the doctrine of catholic and secondary security rights is that where Creditor 1 has a security right over several assets and Creditor 2 has a lower ranking security right over some of these assets, Creditor 1 must enforce its security right in the way least prejudicial to Creditor 2.

[48] With the exception of the floating charge. See *Forth & Clyde Construction Co Ltd v Trinity Timber & Plywood Co Ltd* 1984 SLT 94.

[49] For example, the debtor (if a separate person).

[50] For example, NZ PPSA 1999 s 25(1). For discussion, see Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 116–118. Good faith is also a general principle of the DCFR. See DCFR I.–1:102(3)(b) and I.–1:103.

[51] See A D M Forte (ed), *Good Faith in Contract and Property Law* (1999).

[52] See *Smith v Bank of Scotland* 1997 SC (HL) 111 (duty of security holder to act in good faith). Rights in security here includes cautionary obligations. See G L Gretton, "Sexually Transmitted Debt" 1997 SLT (News) 195 and K G C Reid and G L Gretton, *Conveyancing 2014* (2015) 184–189. Another area of doubt is whether the so-called offside goals rule applies as between holders of rights in security. See Reid, *Property* para 697.

[53] See also M Raczynska, "A new model law of secured transactions: worldwide modernisation in the making?" 2014 Journal of International Finance and Banking Law 697 at 699–700 criticising the use of the term "good faith" in the then draft UNCITRAL Model Law on Secured Transactions.

27.35 Later we deal with the more specific duty of the secured creditor to obtain the best price (or equivalent) reasonably obtainable when realising the encumbered property.[54]

27.36 We recommend:

> **129. In enforcing a pledge a secured creditor should have a duty to conform with reasonable standards of commercial practice. This duty should be to the provider and third parties with an interest in how the pledge is enforced.**
>
> (Draft Bill, s 68(4))

Pledge Enforcement Notice

General

27.37 In the Discussion Paper we expressed the view that the secured creditor would require to serve some form of formal notice on the provider before being allowed to enforce the new security right over moveable property.[55] Such notices are familiar in Scotland because of their use in relation to standard securities.[56] We suggested also that the notice would require to be registered.[57] On reflection we do not think that such notices should be registered. This is the general position under UCC–9, the PPSAs, the DCFR, the UNCITRAL Model Law on Secured Transactions and indeed for standard securities. While the Keeper favoured registration, it was opposed by another of our consultees, Dr Hamish Patrick.

27.38 We think that the enforcement notice should be known as a "Pledge Enforcement Notice". But in consumer cases it would not be the only notice which would be required.

Consumers

27.39 As mentioned above,[58] the Consumer Credit Act 1974 has protections which apply to the grant of any security right by a consumer. In addition, there are requirements in the Financial Conduct Authority's source book dealing with consumer credit (known as "CONC").[59] These would automatically apply to statutory pledges. As noted above the enforcement of possessory pledges subject to the 1974 Act is regulated by specific provisions in that Act and therefore is outwith the scope of our enforcement provisions.[60]

27.40 The approach of the 1974 Act is to regulate certain consumer credit agreements, namely those between an "individual ("the debtor") and any other person ("the creditor").[61] Such an agreement is known as a "regulated agreement".[62] An "individual" includes a partnership consisting of two or three persons, not all of whom are bodies corporate; and an

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[54] See para 28.5 below.
[55] Discussion Paper, para 16.66.
[56] Conveyancing and Feudal Reform (Scotland) Act 1970, ss 19–23A.
[57] Following the precedent of the EBRD Model Law art 22.
[58] See para 27.15 above.
[59] The sourcebook is available at https://www.handbook.fca.org.uk/handbook/CONC/2/.
[60] See para 27.17 above.
[61] Consumer Credit Act 1974 s 8(1).
[62] Consumer Credit Act 1974 s 8(3).

unincorporated association which does not entirely consist of bodies corporate.[63] Therefore, importantly, business loans to sole traders and small partnerships are regulated agreements.

27.41 But certain categories of agreement are exempted. Two are perhaps most relevant for present purposes. The first is business loans of more than £25,000.[64] The second is loans to "high net worth" individuals of more than £60,260.[65] Broadly speaking, individuals are of "high net worth" if they have a net income of £150,000 or more, or assets of £500,000 or more (excluding a home or pension). For this exception to apply, debtors must make a declaration to waive the usual protections and obtain a statement from an accountant giving details of their income or assets.

27.42 In respect of a regulated agreement which is not exempt, there is a requirement for a default notice to be served on the debtor[66] at least 14 days prior to taking any enforcement steps.[67] This requirement would apply to the statutory pledge, in the same way as it applies to other security.[68] This means that for such statutory pledges there is a delay prior to enforcement in the interests of debtor protection. In other cases, enforcement can proceed immediately on the notice being served.

Other persons to be notified

27.43 We consider that an enforcement notice should also be served on holders of other rights in security in the encumbered property or creditors who have executed diligence against it, to let them know that enforcement is to take place. But this duty should only apply in so far as the secured creditor knows or can be reasonably be expected to know of the other right in security or the diligence. Other security rights would often be discoverable from either the RSP or Companies Register. But the fact that someone has executed diligence may be less apparent. Finally, we consider that it should also be necessary to send the notice to any persons with statutory duties in relation to the provider's property who are prescribed for this purpose. We have in mind insolvency officials.

Forms of notice

27.44 We consider that the Scottish Ministers should have the power to prescribe different forms of Pledge Enforcement Notice for different types of provider. We expect that the notice would have more extensive wording in consumer cases, advising the provider of the statutory pledge with information about obtaining advice in relation to the notice.[69] The form for use in non-consumer cases is likely to be briefer. The secured creditor should be required to use the statutory form with only minor deviation.

27.45 We therefore recommend:

130. (a) Before taking any steps to enforce a pledge the secured creditor should require to serve a notice on:

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[63] Consumer Credit Act 1974 s 189(1).
[64] Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (SI 2001/544) art 60C(3).
[65] Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (SI 2001/544) art 60H.
[66] In most cases the debtor and the provider of the statutory pledge would be the same person.
[67] Consumer Credit Act 1974 ss 87 and 88.
[68] For the definition of "security" see the 1974 Act s 189(1).
[69] The width of the definition of "consumer" would be a matter for the Scottish Ministers to consider. As we have noted, the 1974 Act definition is wider than that under the Consumer Rights Act 2015.

(i) the provider,

(ii) the holder of any right in security over all or part of the encumbered property,

(iii) any creditor who has executed diligence against all or part of the encumbered property, and

(iv) any prescribed person who has statutory duties in relation to the provider's estate.

(b) But the duty in cases (ii) and (iii) is to be waived if the secured creditor does not know and cannot reasonably be expected to know of the right in security or diligence.

(c) Such a notice is to be known as a "Pledge Enforcement Notice" in, or as nearly as may be in, such form as may be prescribed.

(d) The Scottish Ministers should have the power to prescribe different forms for different categories of provider.

(e) If by virtue of the Consumer Credit Act 1974, a default notice must be served on the provider, the requirements of that Act in relation to such a notice should require to be satisfied before a Pledge Enforcement Notice can be served.

(Draft Bill, s 69)

Whether court order required for enforcement

27.46 The question of whether a court order should be required to enforce a pledge is one of balance. On the one hand, requiring judicial involvement increases costs and lengthens the enforcement process. On the other hand, the involvement of the court protects the provider from a secured creditor who in fact is enforcing illegitimately.

27.47 In the case of standard securities, the position since the Home Owner and Debtor Protection (Scotland) Act 2010 came into force is that a court order is normally required for enforcement in respect of residential properties.[70] In contrast a court order is not required for non-residential properties. Further, in residential cases the court can only allow enforcement if certain pre-action requirements are complied with and it is reasonable in the circumstances of the case to do so.[71]

27.48 Under the Consumer Credit Act 1974 the rule, as mentioned earlier, for regulated hire-purchase and conditional sale agreements is that a court order is required to recover the goods where there has been default under the agreement, provided that the debtor has paid at least one third of the price.[72] This rule has been carefully reviewed by the Law Commission for England and Wales as part of its Report on Bills of Sale, in which it

[70] Conveyancing and Feudal Reform (Scotland) Act 1970, ss 20(2A) and 23(4). See K G C Reid and G L Gretton, *Conveyancing 2010* (2011) 150–155.
[71] Conveyancing and Feudal Reform (Scotland) Act 1970 s 24(5).
[72] Consumer Credit Act 1974 s 90. See para 27.23 above.

recommends the replacement of bills of sale with "goods mortgages". Its recommendation is that there should be an "opt-in procedure" under which debtors who have repaid one third of their loan could require the secured creditor to obtain court permission to enforce. If the debtor did not opt in no court authorisation would be required. The Commission concluded: "On balance, we have reached the conclusion that court oversight is beneficial, but only to those who actively engage with the process by opting in."[73]

27.49 For possessory pledges regulated by the 1974 Act, which are outwith our scope here, there is a statutory power of sale without the need for court involvement.[74] For other possessory pledges, as we noted in Chapter 25 above, the default position currently is that a court order is required but the parties can agree an express power of sale.

27.50 We believe that the general rule should be that court authorisation should not be required to enforce a pledge. Of course it would always be open to a provider to seek the assistance of the court, for example by seeking an interdict, if the secured creditor acts unlawfully.

27.51 For private individuals, however, we consider that a court order should be required. But we think that "individual" should be defined more narrowly than in the 1974 Act and exclude businesses. Thus a court order should not be required where the provider is a sole trader and the enforcement is against assets used wholly or mainly for the purposes of the provider's business. Our view also is that there should not be a threshold such as less than one third of the debt having being paid where no court order is required. There may be legitimate circumstances of personal hardship where little has been repaid and the provider/debtor could take advantage of their rights under the 1974 Act[75] if the matter requires to go to court. In its response to our draft Bill consultation of July 2017 the Faculty of Advocates questioned the need for a court order if this was a "mere formality". However, in addition to the possibility of exercising rights under the 1974 Act, the need for court involvement would ensure that there was only enforcement in the case of genuine default on the secured obligation.

27.52 We have given careful consideration as to whether providers should require to "opt in" for a court order to be required. On balance, we have decided in the interests of debtor protection that it would be preferable for there to be the ability for the provider to "opt out".[76] After the pledge becomes enforceable the provider should be able to agree in writing that court authorisation is not required.[77] In practice this rule would normally be encountered in relation to statutory pledges, as enforcement of possessory pledges by individuals will usually be regulated by the 1974 Act. Furthermore, given the restrictions which we recommended earlier in relation to the grant of statutory pledges,[78] the asset most likely to be involved is a motor vehicle.

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[73] Law Commission, Bills of Sale (Law Com No 369, 2016) para 7.48.
[74] Consumer Credit Act 1974 s 121 and the Consumer Credit (Realisation of Pawn) Regulations 1983 (SI 1983/1568).
[75] Such as seeking a time order under s 129. This provision gives sheriffs wide powers to alter the rate and time of payments. See further W C H Ervine, *Consumer Law in Scotland* (5th edn, 2015) paras 8-151 to 8-153.
[76] This was the view of those representing consumer groups who responded to the Law Commission's Bills of Sale consultation. See Law Com No 369 para 7.47.
[77] This is the position under the DCFR Book IX.–7:103(2).
[78] See paras 19.36–19.51 above.

27.53 There is of course a strong argument that those who fail to opt out may be very unlikely to engage with the court.[79] It would therefore be crucial that the form of Pledge Enforcement Notice prescribed for individuals should set out as clearly as possible the provider's rights. The notice might also include the possibility for consent to extra-judicial enforcement being given by returning part of the form to the creditor duly signed. This would enable enforcement to be carried out cheaply. Before prescribing the forms we would expect the Scottish Ministers to discuss drafts of these with consumer groups.

27.54 We recommend:

131. (a) A court order should not generally be required to enforce a pledge.

(b) Such an order should be required where the provider of a pledge is an individual unless:

(i) after the pledge becomes enforceable, the provider and the secured creditor agree in writing that it may be enforced without such an order, or

(ii) the provider being a sole trader, enforcement is against property used wholly or mainly for the purposes of the provider's business.

(Draft Bill, s 70(1))

Residential moveable property

General

27.55 Occasionally a statutory pledge might be granted over a large item of corporeal moveable property which is someone's home. The main examples would be boats and caravans. As a matter of law, it is likely that static caravans would be regarded as heritable and therefore could not be the subject of a statutory pledge.[80]

Occupancy rights

27.56 The Matrimonial Homes (Family Protection) (Scotland) Act 1981 and the Civil Partnership Act 2004 provide that where the home of spouses or partners is owned solely by one of them, the other has occupancy rights in it.[81] Under the 1981 Act the home is referred to as a "matrimonial home" and under the 2004 Act it is referred to as a "family home".[82] These definitions include caravans (including those which are mobile) and houseboats.

27.57 The legislation protects the spouse or partner who does not have ownership from any "dealing" in relation to the property, including the grant of a heritable security.[83] Such spouses or partners are referred to as being "non-entitled". Their occupancy rights are

[79] Law Com No 369 para 7.48.
[80] Cf *Christie v Smith's Executrix* 1949 SC 572.
[81] Matrimonial Homes (Family Protection) (Scotland) Act 1981 s 1; Civil Partnership Act 2004 s 135(1).
[82] Matrimonial Homes (Family Protection) (Scotland) Act 1981 s 22; Civil Partnership Act 2004 s 101.
[83] Matrimonial Homes (Family Protection) (Scotland) Act 1981 s 6; Civil Partnership Act 2004 s 106.

unaffected unless they have consented to the dealing. We think that the legislation should be amended to make it clear that the definition of "dealing" includes the grant of a statutory pledge. Further, in the interests of consistency, the provisions protecting heritable creditors who have acted in good faith and have received false documentation in relation to occupancy rights, such as a forged consent, should apply. These enable the creditor to seek a court order requiring a non-entitled spouse or partner who is in occupation of the home to make any payment due by the other spouse or partner in respect of the loan.[84]

27.58 We recommend:

132. (a) The definitions of "dealing" in the Matrimonial Homes (Family Protection) (Scotland) Act 1981 and the Civil Partnership Act 2004 should be amended so as to include the grant of a statutory pledge.

(b) The protections conferred by the Matrimonial Homes (Family Protection) (Scotland) Act 1981 and the Civil Partnership Act 2004 on heritable creditors who have acted in good faith should be amended so as to apply to secured creditors of statutory pledges.

(Draft Bill, s 58(1) & (7) to (12))

Special rules for enforcement

27.59 In general terms we think that the same broad policies should apply to enforcement of a statutory pledge as in the case of a standard security over someone's home.[85] But the legislative scheme for enforcement under the standard security legislation is complex. We will be reviewing this as part of our forthcoming project on heritable securities. The likelihood of a corporeal moveable being someone's home is small. A wealthy individual who owns a boat and falls on hard times is far more likely to sell the boat than move into it. We consider therefore that the scheme for moveable property can be less complex.[86]

27.60 Our view is that a special form of Pledge Enforcement Notice should have to be served on any occupier of the encumbered property. The Scottish Ministers would have power to prescribe different forms for different occupiers. For example, a boat might be rented out to a business merely to provide storage facilities.

27.61 We consider that a court order should normally be required where the property is someone's sole or main residence.[87] The Pledge Enforcement Notice would explain the occupier their rights in relation to this.

27.62 In our view there should be an exception to the need for a court order when, after the security becomes enforceable, the relevant parties agree in writing that such an order is not required. These parties would be (a) the person whose sole or main residence the property is; (b) the provider, if different from that person; and (c) the secured creditor.

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[84] Matrimonial Homes (Family Protection) (Scotland) Act 1981 s 8; Civil Partnership Act 2004 s 108.
[85] On which, see generally G L Gretton and K G C Reid, *Conveyancing* (4th edn, 2011) para 22-35.
[86] According to the Scottish edition of *The Times*, 29 April 2017 in 2016 there were 111 houseboats with residential moorings in Scotland.
[87] Cf Conveyancing and Feudal Reform (Scotland) Act 1970 s 20A(2A)(a) and 23(4)(a)(i).

27.63 The court would require to be satisfied that enforcement is reasonable in all the circumstances of the case before it could grant an order.[88] These circumstances should include those which are specified in the standard security legislation.[89] We recommend:

133. (a) Before taking any steps to enforce a statutory pledge the secured creditor should be required to serve a special form of Pledge Enforcement Notice on any occupier of the encumbered property or part of it.

(b) A court order should be required for enforcing a statutory pledge as regards encumbered property which is the sole or main residence of an individual (whether or not the individual is the provider of the security) unless:

(i) after the statutory pledge becomes enforceable the secured creditor, the provider and (if the individual is not the provider) the individual agree otherwise, and

(ii) the agreement is a written agreement.

(c) The court should not grant an order unless satisfied that enforcement is reasonable in all the circumstances of the case.

(d) Those circumstances should include:

(i) the nature of, and reason for, the default by virtue of which authority to enforce is sought,

(ii) whether the person in default has the ability to remedy the default within a reasonable time,

(iii) whether the secured creditor has done anything to remedy the default,

(iv) whether it is, or was, appropriate for the person in default to take part in a debt payment programme approved under Part 1 of the Debt Arrangement and Attachment (Scotland) Act 2002, whether the person in default is taking part, or has taken part, in such a programme, and

(v) whether reasonable alternative accommodation is available for (or can be expected to be available for) the individual whose sole or main residence is the property.

(Draft Bill, ss 69(1)(e) and 70(2), (4) & (5))

[88] Cf Conveyancing and Feudal Reform (Scotland) Act 1970 s 24(5)(b).
[89] Conveyancing and Feudal Reform (Scotland) Act 1970 s 24(7).

Protection of secured creditor in relation to occupancy rights of spouse or partner

27.64 We have thus far considered the Matrimonial Homes (Family Protection) (Scotland) Act 1981 and the Civil Partnership Act 2004 in the context of statutory pledges being granted over caravans and houseboats etc.[90] Here we discuss an issue in relation to where a statutory pledge has been granted over an item of moveable property within a matrimonial or family home.

27.65 The 1981 and 2004 Acts enable a spouse or partner with occupancy rights (the "non-entitled spouse or partner") in such a home to apply to the court for an order granting them possession or use of any furniture and plenishings within the home. But such an order is not to prejudice any third party in relation to the non-performance of any obligation under a hire-purchase or conditional sale agreement in relation to that property.[91] This is subject to another provision enabling the spouse or partner with occupancy rights to perform obligations due by the other spouse or partner ("entitled spouse or partner").[92] The policy is to enable creditors to enforce their rights under hire-purchase and conditional sales contracts. We consider that the same protection should apply to a secured creditor who has taken a statutory pledge over such furniture or plenishings. In practice, however, because of the value threshold which we recommend elsewhere for providers of statutory pledges who are individuals we do not expect that the provision would be frequently engaged.[93]

27.66 It might also be asked whether non-entitled spouses and partners should not be prejudiced by the grant of a statutory pledge over furniture or plenishings unless they have consented to it. But the 1981 and 2004 legislation offers protections from dealings with the *home* without consent rather than with the *contents*. Thus under the current law the entitled spouse or partner could pawn an item of furniture without the consent of the non-entitled spouse or partner and the pawn would be effective against them.

27.67 We recommend:

> **134. The protections conferred by the Matrimonial Homes (Family Protection) (Scotland) Act 1981 and the Civil Partnership Act 2004 in relation to creditors under hire-purchase and conditional sale agreements in relation to furniture and plenishings should be extended to include secured creditors of statutory pledges.**
>
> (Draft Bill, s 58(1) to (6))

Secured creditor's right to take possession of or immobilise corporeal property

General

27.68 For a possessory pledge, as the name indicates, the secured creditor does not need to seize the property in order to realise it. Possession is already held. But for a statutory pledge it would be the provider who would normally be in possession. There requires to be a mechanism by which the secured provider can take hold of the asset. Here debtor

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[90] See paras 27.55–27.58 above.
[91] Matrimonial Homes (Family Protection) (Scotland) Act 1981 s 3(2); Civil Partnership Act 2004 s 103(2).
[92] 1981 Act s 2; 2004 Act s 102.
[93] See paras 19.36–19.51 above.

protection is important. The circumstances under which possession can be taken require to be carefully regulated.

27.69 The general rule should be that once the secured creditor in a statutory pledge has served a Pledge Enforcement Notice there should be an entitlement to take possession of the encumbered property. For some assets such as boats or machinery it may be more convenient for the secured creditor to immobilise the property or take other reasonable steps to ensure that it is not disposed of or used in an unauthorised way.

27.70 We think that the secured creditor should be able personally (or through agents or employees) to take possession of or immobilise the property with the consent of the provider or of any third party such as a warehouser who is holding the property. But that consent should require to be given after default, otherwise the risk is that it is written into any security agreement that the provider will give consent. Where consent is not forthcoming the secured creditor should require to obtain a court order to take action personally in relation to the property. The court may wish to set down conditions as to how possession is to be taken or immobilisation carried out.

27.71 Obtaining a court order of course takes time and costs money. We therefore consider that possession might also be taken or immobilisation carried out by an "authorised person" acting on behalf of the secured creditor. In response to our consultation question on enforcement, Dundas & Wilson stated: "We believe that it may be desirable (from a public policy perspective) that . . . agents [appointed to enforce a statutory pledge should] be required to be [insolvency practitioners] to ensure standards of behaviour – the regulation of such persons is already onerous."

27.72 In our view the case for regulation is a strong one, in particular in a non-corporate context, where the property of individuals is being seized on default. We consider that there should be three categories of authorised person. The first is messengers-at-arms and sheriff officers. These are officers of the court and therefore under judicial supervision.[94] They are experienced in enforcing debts against assets through their work in relation to diligence (the legal process used by unsecured creditors against assets). It is already possible for them to carry out extra-judicial debt collection subject to certain conditions.[95]

27.73 The second is qualified insolvency practitioners. They are experienced in enforcing floating charges and more generally dealing with the assets of distressed companies. Importantly, they are also subject to detailed regulation.[96] We would anticipate that the secured creditor is more likely to appoint an insolvency practitioner in corporate cases where the same statutory pledge encumbers a range of assets.

27.74 Thirdly, we consider that the Scottish Ministers should be able to prescribe other persons who may act as agents. This would provide the legislation with some flexibility.

27.75 In the case of a large corporeal moveable such as a boat there may be a need to remove any individual present in the property. Under the recommendations which we make

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[94] See S Cowan, *Scottish Debt Recovery: A Practical Guide* (2011) para 6-03. As the name implies, sheriff officers act under the supervision of the Sheriff Court. Their equivalent in the Court of Session are messengers-at-arms. It is common for individuals to hold both offices.

[95] Debtors (Scotland) Act 1987 s 75(1)(f). See Cowan, *Scottish Debt Recovery* para 6-05.

[96] Insolvency Act 1986 ss 388–398.

above a court order would be required first if the property is someone's sole or main residence. We consider that removing individuals should only be carried out by authorised persons.

27.76 We therefore recommend:

135. (a) The following rules should apply in relation to corporeal property in respect of which a secured creditor in a statutory pledge has served a Pledge Enforcement Notice.

(b) The secured creditor should be entitled:

(i) to take possession of the property, or

(ii) to take any reasonable steps necessary to ensure, whether or not by immobilising the property, that it is not disposed of or used in an unauthorised way.

(c) The secured creditor should be able to take such possession, or such steps:

(i) personally if authorised to do so by the court but otherwise only with the consent of the provider given after default, and of any third party who is in direct possession of, or has custody of, the property, or

(ii) through the agency of an authorised person.

(d) The secured creditor should be entitled, in taking possession of the encumbered property to remove any individual from it, but only through the agency of an authorised person.

(e) An "authorised person" should mean:

(i) a messenger-at-arms or sheriff officer,

(ii) a person qualified to act as an insolvency practitioner, or

(iii) such other person as the Scottish Ministers may by regulations specify.

(Draft Bill, s 71(1) to (4) and (8) to (9))

Encumbered property in the possession of higher or equal ranking creditors

27.77 It is possible that the encumbered property may be in the possession of another secured creditor or a creditor who has carried out diligence against it. Thus for example, Carol, who is enforcing a statutory pledge over an asset owned by Andrew, may find that it is in the possession of Ben, the holder of a higher ranking statutory pledge who is also in the process of enforcing his security right.

27.78 Where the other creditor has a higher or equal ranking we consider in principle that it should not be possible for possession to be recovered from that other creditor.[97] This is because that creditor has a higher or equal entitlement to the property and should be entitled to realise the asset. It should of course be possible for possession to be taken with the consent of the other creditor. Alternatively, there should be a right to take possession of the property or immobilise it with the authorisation of the court (personally if the court authorises this or by means of an authorised person). Thus, depending on the precise circumstances, the court may be willing to authorise the taking of possession if the other creditor is unreasonably delaying in realising the property.

27.79 We recommend:

136. (a) The secured creditor should not have an entitlement to take possession of the encumbered property or to take the steps set out in the previous recommendation if the property is in the possession of a person:

(i) who has a right in security over the property, or over any part of the property, being a right in security which has priority over, or ranks equally with, the pledge to which the Pledge Enforcement Notice relates, or

(ii) who has executed diligence against the property, or against any part of the property, and by virtue of that diligence has priority in ranking over, or ranks equally with, that pledge.

(b) But in these circumstances the secured creditor may take possession or take these steps:

(i) with the consent of the person who has the right in security over the property, or has executed diligence against it,

(ii) if authorised by the court, through the agency of an authorised person, or

(iii) personally, if authorised to do so by the court.

(Draft Bill, s 71(6) & (7))

Secured creditor's right to take possession of certificate of financial instrument

27.80 The secured creditor may also need to obtain possession of financial instrument certificates. Similar rules should apply as for corporeal property, although clearly there is no need for powers of immobilisation. Possession should be able to be taken with consent, or through the agency of an authorised person, or personally where the court authorises this. There should be equivalent restrictions as for corporeal property where the instrument is in

[97] See the draft Floating Charges and Moveables Securities (Scotland) Bill, cl 17(1)(a).

the possession of a higher or equal ranking creditor. In practice, however, we understand that diligence against financial instruments is unusual.

27.81 We recommend:

137. The taking of possession of financial instrument certificates by the secured creditor should be subject to similar rules as the taking of possession of corporeal property.

(Draft Bill, s 72)

Chapter 28 Enforcement of pledge (2)

Introduction

28.1 This chapter considers further issues in relation to enforcement of pledges, in particular realisation of the encumbered property. We set out the remedies which we recommend should be available, namely sale, lease, licensing (in the case of intellectual property) and appropriation. Finally, we look at the secured creditor's liability for breach of duty in relation to enforcement.

Secured creditor's entitlement to sell

28.2 The standard method of realising encumbered assets is to sell them. Clearly an enforcing creditor should have the right to do this. Of course, as discussed in the previous chapter, first the enforcing creditor would require to have served a Pledge Enforcement Notice and, where applicable, obtained a court order authorising enforcement.

28.3 The sale could be by private agreement or by public auction. Requiring a court to supervise the sale would in our view unnecessarily increase costs. Under the standard security legislation there is a requirement to advertise before the sale.[1] We understand from our advisory group that because of this rule where land held by a company is subject to both a floating charge and a standard security, sale is effected under the floating charges legislation because it does not have a requirement for advertisement. This reduces time and costs, which ultimately would be borne by the provider. We note that legislation in other jurisdictions and the DCFR and UNCITRAL Model Law on Secured Transactions do not impose a specific duty to advertise.[2] We are not convinced that advertisement should be an express requirement for pledges under the new scheme, because the provider can be protected in other ways.

28.4 First, we recommended earlier that the secured creditor must conform with reasonable standards of commercial practice.[3] This general duty would apply to how sale is effected.

28.5 Secondly, in common with the standard security legislation and comparator legislation on security over moveable property, the secured creditor in selling the property would require to take all reasonable steps to ensure that the price obtained is the best reasonably obtainable.[4] This is a general rule of rights in security law and is required to protect providers. Imagine that David has granted a statutory pledge over a painting worth £100,000 in favour of Eric for a loan of £60,000. If Eric requires to enforce, his personal interest is only in obtaining the £60,000 owed to him. But it would not be fair to David for the painting to be sold for that amount when it is worth £100,000. He is entitled to receive the

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[1] Conveyancing and Feudal Reform (Scotland) Act 1970 s 25.
[2] NZ PPSA 1999 ss 109 and 110; Australian PPSA 2009 s 128; DCFR IX.–7:211 (although private sale is only permitted by agreement with the provider); and UNCITRAL Model Law on Secured Transactions art 78.
[3] See paras 27.32–27.36 above.
[4] Conveyancing and Feudal Reform (Scotland) Act 1970 s 25; NZ PPSA 1999 s 110; Australian PPSA 2009 s 131. DCFR IX.–7:212 appears to have a slightly lower standard of a "commercially reasonable price".

£40,000 of remaining value in the painting. Depending on the circumstances it may well be necessary for the secured creditor to advertise to fulfil the duty to obtain the best price reasonably obtainable.[5] In other cases, where the asset has a clear market value (such as certain financial instruments) advertising may not be necessary.

28.6 It may be that the secured creditor wishes to buy the encumbered property or some of it. We think that this should be possible but only in restricted circumstances to ensure that proper value is achieved. We recommend a rule based on the Saskatchewan PPSA[6] under which the secured creditor can only buy the property if the sale is by public auction and the price bears a reasonable relationship to market value.[7] Alternatively, where the property is tradeable on a public market such as the Stock Exchange and its market value is verifiable the secured creditor should be able to purchase it at that value.

28.7 Once the sale has taken place the secured creditor should require to hold the proceeds in trust until these are applied towards the obligations secured on the property (whether by that statutory pledge or other security rights) and any surplus returned to the provider. This means that the proceeds would be protected if the secured creditor becomes insolvent as the proceeds would be outwith the secured creditor's ordinary patrimony.

28.8 We recommend:

138. (a) Where a pledge is being enforced, the secured creditor should be entitled to sell all or any of the encumbered property.

(b) The secured creditor, in selling the property, should require to take all reasonable steps to ensure that the price obtained is the best reasonably obtainable.

(c) The secured creditor should be entitled to purchase all or any of the property only if the sale is by public auction and if the price bears a reasonable relationship to market value.

(d) If the property is tradeable in a public market in which the current market value is verifiable the secured creditor should be entitled to purchase all or any of the property only in that market and for market value.

(e) Any proceeds derived from the sale should require to be held in trust until applied by the secured creditor.

(Draft Bill, s 73)

Effect of sale

28.9 Although the provider is not a party to the sale, the secured creditor requires to be enabled by the law to transfer the provider's title to the property to the purchaser. And the purchaser should acquire the property unencumbered by the pledge.

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[5] See Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 398–399.
[6] Saskatchewan PPSA 1993 s 59(13).
[7] A public auction will not necessarily achieve market value, for example, if few bidders attend.

28.10 It is a general principle of rights in security law that the purchaser also takes the property free of any lower ranking security rights or diligence.[8] The lower ranking creditors are in principle compensated in respect of the loss of their rights by receiving a share of the proceeds of the sale. But that of course is only if there are sufficient proceeds. The lower-ranking secured creditors will, however, be aware of this risk when they take their security rights and have the opportunity to lower their exposure by charging higher interest on the debt.[9]

28.11 The position as regards equal ranking rights or diligence appears to be less clear internationally, but in line with the position for standard securities we consider that the purchaser should also take free of these.[10]

28.12 In contrast the purchaser would take the property subject to the rights of higher ranking creditors. The existence of such rights, however, may make sale of the property difficult as purchasers will naturally want to acquire unencumbered ownership. Therefore, following the approach of the DCFR,[11] we think that it should be possible for agreement to be made with the higher ranking creditor, the effect of which would be that it would receive its share of the proceeds according to its ranking and the purchaser would therefore take the property free of the pledge.

28.13 We recommend:

139. Where the secured creditor sells encumbered property on enforcement the purchaser should acquire the property unencumbered by:

(a) the pledge,

(b) any right in security or any diligence ranking equally with, or postponed to, the pledge, and

(c) any right in security or any diligence which has priority in ranking over the pledge, but only if the holder of that right in security, or as the case may be the creditor who executed that diligence, consented to the sale.

(Draft Bill, s 74)

Secured creditor's entitlement to let

28.14 We think that the secured creditor should in principle be entitled to recover the secured debt by means of letting (leasing) the property and receiving rent payments. The Murray Report recommended such a remedy.[12] It is also available under the Belgian Pledge

[8] Conveyancing and Feudal Reform (Scotland) Act 1970 s 26(1); NZ PPSA 1999 s 115; Australian PPSA 2009 s 133; DCFR IX.–7:213.
[9] Drobnig and Böger, *Proprietary Security in Movable Assets* 751–752.
[10] Conveyancing and Feudal Reform (Scotland) Act 1970 s 26(1).
[11] DCFR IX.–7:213(2).
[12] Although it referred to it as "hire". See the draft Floating Charges and Moveable Securities (Scotland) Bill, cl 17(3)(a) appended to the Murray Report. While "hire" is the traditional term for a lease of corporeal moveables, the word "lease" is commonly used nowadays too, not least in the context of finance leases.

Act, the DCFR, the UNCITRAL Model Law and some PPSAs.[13] The approach sometimes taken is that letting is only permissible where the parties have agreed on this. In the interests of commercial flexibility we think that the default position should be that the secured creditor can let the property, but the parties should be able to exclude this by means of written agreement.

28.15 As for sale, the secured creditor should require to take all reasonable steps to ensure that the rental income obtained is the best reasonably obtainable. Thus a houseboat which could command a rental of £1,000 a month should not be leased for £100 per month. The greater the income generated the faster the secured debt will be recovered. Again, as for sale, the secured creditor should hold the income in trust until it is applied towards the obligations secured on the property. We recommend:

140. (a) Where a pledge is being enforced it should be competent for the secured creditor to let all or any of the encumbered property.

(b) The secured creditor in letting the property should require to take all reasonable steps to ensure that the rental income obtained is the best reasonably obtainable.

(c) The rental income obtained should be held in trust by the secured creditor until applied towards the satisfaction of the secured obligation.

(d) The provider and the secured creditor should be able to agree that the right to let is excluded in respect of all or any of the encumbered property. Such an agreement should require to be set out in writing.

(Draft Bill, s 75)

Secured creditor's entitlement to grant licence over intellectual property

28.16 In our review of comparative legislation we noted that the Australian PPSA makes specific provision for enforcement in the case of intellectual property by allowing the secured creditor to grant a licence of this.[14] Other comparators such as the DCFR do not have such a provision.[15] On one view a licence is merely a form of lease and we have already recommended that the secured creditor should be entitled to grant a lease.[16] The view of our advisory group, however, was that the best approach was to make express provision. There is a potential legislative competence issue here because the law on intellectual property is generally reserved to the UK Parliament. But as the purpose of the provision is to enable enforcement of a security right, we take the view that a provision would be within the competence of the Scottish Parliament.[17]

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[13] Belgian Pledge Act of 11 July 2013 art 55 (non-consumer cases) (which provides for art 47 of the new Book III title XVII of the Civil Code); DCFR IX.–7:207(1)(b); UNCITRAL Model Law on Secured Transactions art 78; Saskatchewan PPSA 1993 s 59(3)(d); Australian PPSA 2009 s 128(2)(b).
[14] Australian PPSA 2009 s 128(2)(c).
[15] But compare the UNCITRAL Model Law on Secured Transactions art 78, which expressly permits licensing.
[16] See paras 28.14–28.15 above.
[17] See para 1.47 above.

28.17 Our view is that the provision should work broadly in the same way as that on enforcement by leasing the encumbered property. It should be open to the parties to exclude licensing as a remedy by means of written agreement. The secured creditor should only be able to grant a licence to the extent that the provider was able to grant such a right.[18] Where a licence is granted the secured creditor should be required to take all reasonable steps to ensure that the rental income obtained is the best reasonably obtainable. The income should then be held in trust until applied towards satisfaction of the secured obligation.

28.18 We recommend:

141. (a) Where a statutory pledge over intellectual property is being enforced it should be competent for the secured creditor to grant a licence over all or any of that property (but only if and to the extent that the provider is entitled to grant such a licence).

(b) The secured creditor in granting a licence should require to take all reasonable steps to ensure that the rental income obtained is the best reasonably obtainable.

(c) The income obtained should be held in trust by the secured creditor until applied towards the satisfaction of the secured obligation.

(d) The provider and the secured creditor should be able to agree that the right to grant a licence is excluded in respect of all or any of the intellectual property encumbered by the statutory pledge. Such an agreement should require to be set out in writing.

(Draft Bill, s 76)

Secured creditor's entitlement to protect and maintain etc. the encumbered property

28.19 We consider that the secured creditor should be entitled to have management powers in relation to the encumbered property. There should be the right to protect, maintain and manage the property and to take steps to preserve its value. For example, certain assets would require to be stored under particular conditions pending realisation or they may deteriorate.

28.20 In our view it would also be helpful to set out in statute a non-exhaustive list of actions that might be taken by the secured creditor, such as exercising voting rights in relation to financial instruments which are encumbered property; insuring the encumbered property; or bringing, defending or continuing legal proceedings in relation to that property. We recommend:

142. (a) A secured creditor who is enforcing a pledge should be entitled to take reasonable steps to protect, maintain and manage the encumbered property and to preserve its value.

(b) Such steps could include:

[18] For example, the provider may have already granted an exclusive licence to another party.

(i) exercising any voting rights in relation to a financial instrument which is encumbered property,

(ii) effecting or maintaining an insurance policy in relation to the encumbered property,

(iii) settling any liability in relation to that property,

(iv) bringing, defending or continuing legal proceedings in relation to that property, and

(v) taking such other steps as the provider, whether before or after the pledge has become enforceable, has agreed may be taken by the secured creditor.

(Draft Bill, s 77)

Application of proceeds from enforcement of pledge

General

28.21 Once the secured creditor has realised the encumbered property from sale, lease or licence, the proceeds obtained require to be applied. We consider now the rules that should apply in relation to this.[19]

Distribution: (a) expenses

28.22 The first thing which the proceeds should be used to meet is the expenses which the secured creditor has reasonably incurred in relation to enforcement. While the standard security legislation limits recovery to "properly incurred"[20] expenses, the Murray Report and comparator legislation allow "reasonable"[21] expenses. We follow that latter approach here. Clearly, "expenses" should be interpreted broadly and include costs incurred in realising the property by sale or otherwise. We think that it would be helpful to make it clear that the secured creditors' costs in taking possession of or immobilising the property, as well as managing it prior to realisation should also be covered.

28.23 After the expenses are paid the remaining proceeds require to be distributed in accordance with the rankings of the security rights or diligence affecting the property.

Distribution: (b) other secured creditors

28.24 As noted above,[22] the default position should be that higher ranking creditors are unaffected by realisation and their rights continue to encumber the property. Accordingly they do not participate in the distribution. But again, as was discussed earlier, this may make realisation – particularly sale - difficult and therefore it should be possible for the

[19] Broadly equivalent rules are found in comparator legislation or instruments. See eg Conveyancing and Feudal Reform (Scotland) Act 1970 s 27; draft Floating Charges and Moveable Securities (Scotland) Bill, cl 19; Australian PPSA 2009 s 140; and DCFR IX.–7:215.
[20] Conveyancing and Feudal Reform (Scotland) Act 1970 s 27(1)(a).
[21] Draft Floating Charges and Moveable Securities (Scotland) Bill cl 19(1)(a); DCFR Book IX.–7:215(5); NZ PPSA 1999 s 16(1) (definition of "future advance") and Australian PPSA 2009 s 18(5).
[22] See para 28.12 above.

higher ranking creditor to agree to the realisation. The property can then be sold unencumbered. In that case the higher ranking creditor must be paid from the proceeds in priority to the secured creditor who is actually enforcing.

28.25 Example 1. Carol is enforcing a statutory pledge over a yacht owned by Ann. There is a prior ranking statutory pledge over it in favour of Bill. Carol is owed £20,000. Bill is owed £30,000. The boat is sold for £100,000. Bill consents to the sale. Carol's expenses are £1,000 and these are paid first, leaving £99,000.

28.26 Next comes Bill's £30,000. But if there were more than one higher ranking creditor who consented to the sale then payment should be in accordance with their respective rankings. The same principle applies to lower ranking creditors and we give an example in that regard below.

28.27 Next comes the secured creditor who is enforcing the pledge. Thus, to continue the example, Carol would receive her £20,000 (leaving £49,000 to be returned to Ann as we will confirm below.[23])

28.28 There may be a secured creditor with a right in security, or a creditor who has executed diligence, which ranks equally with the pledge being enforced. This situation, however, is admittedly unlikely, except in the context of a ranking agreement. But, if it were to arise, the other creditor would be entitled to the same priority as regards the proceeds as the enforcing creditor. If there were insufficient proceeds to pay equal ranking creditors then the payments to them would abate in equal proportions.

28.29 Example 2. Kelvin and Marion have equal ranking statutory pledges over a combine harvester. Kelvin's secured debt is £30,000 and Marion's is £60,000. The ratio of the debts is therefore 1:2. After expenses are deducted, there are proceeds of £48,000 from the sale of the vehicle. Kelvin will get £16,000 and Marion £32,000. In other words, both get approximately one half of what is due to them (in the ratio 1:2 because the amount owed to Marion is double that owed to Kelvin).

28.30 Next come any lower ranking creditors. They must be paid in the order of their ranking.

28.31 Example 3. A patent owned by Henry is the subject of three statutory pledges. The first ranking is held by Ophelia who is owed £3,000. The second ranking is held by Peter, who is owed £2,000. The third ranking is held by Quentin, who is also owed £2,000. Ophelia enforces her security right and after expenses the proceeds are £6,000. Ophelia recovers her £3,000, Peter his £2,000 but Quentin only obtains £1,000 and is an unsecured creditor for the £1,000 shortfall.

Distribution: (c) residue

28.32 Finally, any residue should be returned to the provider. Thus, to complete Example 1 above, the figure which Ann receives is £49,000. If, however, the provider has become insolvent it will be paid instead to the relevant insolvency official.

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[23] See para 28.32 below.

28.33 We recommend:

143. (a) Any proceeds arising from enforcement should be applied:

(i) firstly, in payment of all expenses reasonably incurred by or on behalf of the secured creditor in connection with the enforcement,

(ii) secondly, in payment of the amount due under any right in security over the property from which the proceeds arose, or to a creditor who has executed diligence against that property in accordance with ranking, and

(iii) thirdly, in payment to the provider of any residue.

(b) No payment should be made to a higher ranking creditor unless it has consented to the realisation.

(c) Where payment is to be made to more than one person with the same ranking but the proceeds are inadequate to enable those persons to be paid in full, their payments should abate in equal proportions.

(d) "Expenses" should be defined to include the costs of taking possession of, immobilising and managing the property.

(Draft Bill, s 82(1) to (5) & (10))

Consignation

28.34 Occasionally, it may be unclear to whom payment should be made or it may not be practical to make payment because a person has disappeared. In these circumstances the secured creditor should be required to pay (consign) the money into court for the person appearing to have the best right to that payment.[24] If another creditor with a security right over the property cannot be traced it may not be possible to ascertain what is owed to that person and therefore consignation will not be possible. Ascertainment is easier where there is a residue owed to an absent provider.[25] Consignation should operate as a payment of the amount due and a certificate from the court should be sufficient evidence of that payment. The court would normally be the sheriff court.[26]

28.35 We recommend:

144. (a) Where a question arises as to whom a payment should be made, the secured creditor should be required to:

(i) consign the amount of the payment (so far as ascertainable) in court for the person appearing to have the best right to that payment, and

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[24] See eg Conveyancing and Feudal Reform (Scotland) Act 1970 s 27(2) & (3).
[25] Cf NZ PPSA 1999 s 118.
[26] Unless the sum is sufficiently large that it comes within the jurisdiction of the Court of Session.

(ii) lodge in court a statement of the amount consigned.

(b) Such a consignation should operate as a payment of the amount due and a certificate of the court should be sufficient evidence of that payment.

(Draft Bill, s 82(6) to (9))

Statements

28.36 After applying the proceeds the secured creditor should have to supply relevant parties who have an interest in the matter with a statement as to how this was done.[27] This will enable them to check that the proceeds are applied properly. The parties who we think have an interest are (a) the provider; (b) the debtor in the secured obligation if a person other than the provider; (c) other secured creditors or parties who have executed diligence against the property; and (d) any prescribed persons with statutory duties in relation to the provider's property. For the last of these categories we have in mind insolvency officials. Where the property is sold, a single statement would suffice, but if it is leased or licensed monthly statements would seem appropriate.

28.37 We recommend:

145. (a) The secured creditor should be required, as soon as reasonably practicable, to present:

(i) the provider,

(ii) the debtor in the secured obligation if a person other than the provider,

(iii) any other creditor affected by the enforcement, and

(iv) any prescribed person who has statutory duties in relation to the provider's estate

with a written statement of how the proceeds arising from the enforcement have been applied.

(b) But where the proceeds arise from the letting or licensing of the property a monthly statement should be sufficient.

(Draft Bill, s 82(11) & (12))

Appropriation

Introduction

28.38 Imagine that Jennifer owes Keith £5,000 and grants a statutory pledge over her painting in security of the debt. The painting is worth £100,000. It would be unfair for the

[27] Cf NZ PPSA 1999 s 116.

painting simply to be forfeited to Keith if the debt is not paid because Keith would obtain a £95,000 windfall.[28] Thus while forfeiture was the default remedy for pledge in earlier times, it became replaced by sale, with any proceeds in excess of the debt being returned to the provider. Post-classical Roman law then prohibited forfeiture clauses, that is to say an agreement between the provider and the secured creditor that the property is forfeited on default.[29] The ban on forfeiture clauses was received into modern European countries and English law has a similar rule (equity of redemption).[30]

28.39 Modern comparator legislation, however, does allow forfeiture but in restricted circumstances. Pre-default agreements are still prohibited.[31] But post-default a secured creditor can *appropriate* the asset in satisfaction of the secured obligation if there is no objection from the provider and other creditors.[32] Sale is seen as the primary remedy because it may well fetch more money and therefore the provider and other creditors can veto appropriation. But in some circumstances, such as financial instruments, which have an objectively verifiable market price, a sale will not achieve more and all with an interest may be content for the secured creditor to appropriate at that value.

28.40 We consider therefore that, subject to restrictions, appropriation should be a remedy that is available to the secured creditor. In framing our recommendations here we have drawn on the DCFR.

General

28.41 For a secured creditor to have power to appropriate, in common with the other methods of realisation, they must have first served a Pledge Enforcement Notice. We think that appropriation should be excluded in consumer cases[33] and thus in the case of sole traders should be confined to assets used wholly or mainly for the purposes of the provider's business.

28.42 If the amount to be obtained by the appropriation is greater than the amount secured we think that it should only be possible for the appropriation to take place if the secured creditor holds the excess amount in trust to be applied as if it were proceeds.

28.43 For corporeal property or financial instruments payable to bearer it should be necessary for the secured creditor to have possession prior to appropriating as the general law requires delivery of such assets to the transferee for transfer to take place.[34] For intellectual property and non-bearer financial instruments further steps may be required for the secured creditor to take ownership, such as being entered in a register such as an IP register or the register of a company's shareholders. We recommend:

146. (a) The secured creditor should be entitled to appropriate any or all of the encumbered property in total or partial satisfaction of the secured obligation.

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[28] See also paras 25.14–25.17 and 25.20–25.21 above.
[29] By legislation of Constantine in AD 326. See Codex 8.34.3.
[30] See M Bussani, *Il problema del patto commissorio: studio di diritto comparato* (2000). The classic study in English law is R W Turner, *The Equity of Redemption* (1931).
[31] See eg DCFR IX.–5:101(2).
[32] Under the NZ PPSA 1999 s 120 and the Australian PPSA 2009 s 134 this is known as "retention".
[33] Cf DCFR Book IX.–7:105(3).
[34] But the Sale of Goods Act 1979 does not.

(b) But it should not be competent to appropriate:

(i) the property of an individual unless that person is a sole trader and the appropriation is of assets used wholly or mainly for the purposes of the person's business,

(ii) corporeal property, or a financial instrument payable to bearer, unless it is in the possession of the secured creditor, or

(iii) property the value of which exceeds the amount for the time being remaining due under the secured obligation and the costs of enforcement unless the secured creditor holds the excess amount on trust to be applied as if it were proceeds.

(Draft Bill, s 78)

28.44 The DCFR draws a distinction between cases where (i) there is an agreement as to appropriation between the provider and the secured creditor made prior to default (which is only allowed in restricted circumstances) and (ii) there is no such agreement. We begin with the latter.[35]

Where no pre-default agreement

28.45 The secured creditor should be required to serve notice of its intention to appropriate to parties who have an interest in the matter, namely (a) the provider; (b) the debtor in the secured obligation if a person other than the provider; (c) any person with a right in security over all or part of the property; (d) any person who has executed diligence against all or part of the property; and (e) any prescribed person who has statutory duties in relation to the provider's estate (once again we have in mind here insolvency officials). As regards (c) and (d) the duty should only apply in so far as the secured creditor knows or can reasonably be expected to know of the other right in security or diligence.

28.46 First, the notice should identify the property to be appropriated. For example, a statutory pledge may have been granted over several assets and appropriation is only to take place in respect of one of them. Secondly, it should specify the sum remaining due under the secured obligation and the amount to be obtained by the appropriation.[36] Thirdly, it should state that the addressee has the right to object within 14 days.

28.47 There are various reasons why an addressee would object, although in common with comparator legislation they should not require to have to set out their reasons. The addressee may, for example, consider that sale would achieve a greater amount. It may be a higher ranking creditor who wishes to preserve its priority in relation to the asset. It may not be happy about the amount which the secured creditor wishing to appropriate states is to be obtained by the appropriation. In relation to the last of these, we believe following the

[35] DCFR IX.–7:105 and 7:216.
[36] See DCFR IX.–7:216(d).

DCFR[37] that the appropriation should not be permitted unless the amount to be obtained by it bears a reasonable relationship to the market value of the property.

28.48 Where an addressee of the appropriation notice objects then the appropriation may not proceed. We recommend:

147. (a) Before exercising any right to appropriate property, the secured creditor should require to serve a notice on:

(i) the provider,

(ii) the debtor in the secured obligation if a person other than the provider,

(iii) any other person with a right in security over all or part of the property,

(iv) any person who has executed diligence against all or part of the property, and

(v) any person who has statutory duties in relation to the provider's estate and is prescribed under this paragraph.

(b) But the duty in cases (iii) and (iv) is to be waived if the secured creditor does not know and cannot reasonably be expected to know of the right in security or diligence.

(c) Any notice should require to:

(i) identify the property to be appropriated,

(ii) specify:

(a) the amount for the time being remaining due under the secured obligation, and

(b) the amount to be obtained by the appropriation,

(iii) state that the recipient has a right to object within 14 days of the receipt of the notice.

(d) The appropriation may not proceed unless the amount to be obtained by it bears a reasonable relationship to the market value of the property.

[37] DCFR IX.–7:216(c).

(e) If within 14 days after receiving notice a recipient, by means of a written statement made to the secured creditor, objects to the appropriation, it is not to proceed.

(Draft Bill, s 79)

Where pre-default agreement

28.49 The DCFR permits the provider and the secured creditor to enter into a pre-default agreement as to appropriation in limited circumstances. These are:

> "(a) if the encumbered asset is a fungible asset that is traded on a recognised market with published prices; or
>
> (b) if the parties agree in advance on some other method which allows a ready determination of a reasonable market price."[38]

28.50 The policy behind these two cases is that there is less risk of the property being appropriated below value and prejudice being caused to the provider.[39] An example of the first case would be publicly tradeable shares on a stock exchange. An example of a second case might, in respect of motor vehicles, be prices listed in a particular used car guide. We find the policy of the DCFR here persuasive and recommend similar rules for pledge.

28.51 The provider and the secured creditor should be entitled to enter into a pre-default agreement as to appropriation, but such an agreement would require to be in writing. Such an agreement would only be permissible in respect of two types of property.

28.52 The first type would be fungible assets traded on a specified market, being a market where the prices are published and widely available (whether on payment of a fee or otherwise). The relevant markets would be specified by regulations. A "fungible asset" would be defined as an asset of a nature to be dealt in without identifying the particular asset involved. Financial instruments will often come into this category. Patents and paintings will not.

28.53 The second type would be property in relation to which the parties in their agreement have set out a method of determining a reasonable market price.

28.54 The appropriation would require to be for the published market price or the price determined by the parties, as at the date of the appropriation. If that price exceeded the amount due under the secured obligation, the residue would require to be returned to the provider.

28.55 While the provider, having entered into the agreement, would be bound by it, other parties with an interest would not. Therefore notice of the intended appropriation would require to be given to the same parties as where there is no pre-default agreement. Where, however, the debtor and the provider are not the same person we consider that the debtor is sufficiently protected by the recommendation that a pre-default agreement can only authorise appropriation at market price. Therefore we do not think that the debtor should

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[38] DCFR IX.–7:105.
[39] Drobnig and Böger, *Proprietary Security in Movable Assets* 720.

have a right of objection. But the other parties could object within 14 days of receipt of the notice. Other than a higher ranking creditor which wishes to preserve its priority, we think it unlikely that there would be objection in such circumstances. We recommend:

148. (a) The provider and the secured creditor should be able, before the pledge becomes enforceable, to agree in writing that the secured creditor is entitled to appropriate the encumbered property or part of that property.

(b) Any property to be appropriated in accordance with that agreement must be:

(i) a fungible asset that is traded on a specified market, being a market the prices on which are published and widely available (whether on payment of a fee or otherwise), or

(ii) if it is not such an asset so traded, property as regards which the provider and the secured creditor have, in the agreement, set out a method of readily determining a reasonable market price,

and be appropriated only for the value of its market price as so published or as the case may be as so determined.

(c) Notice should require to be given to the same parties as mentioned in the previous recommendation of the proposed appropriation and other than the provider (or debtor where different from the provider) they should have the right to object within 14 days of receiving the notice.

(d) "Fungible asset" should be defined as an asset of a nature to be dealt in without identifying the particular asset involved, and "specified" as specified for these purposes by the Scottish Ministers by regulations. It should be possible for the regulations to specify different markets or descriptions of market in relation to different kinds of fungible asset.

(Draft Bill, s 80)

Effect of appropriation

28.56 Where the secured creditor exercises the right to appropriate encumbered property, having had no objection from the holders of any other rights in security over the property or creditors who have executed diligence against the property, the secured creditor should acquire an unencumbered title.

28.57 We recommend:

149. Where the secured creditor appropriates encumbered property, the property should be acquired unencumbered by any right in security or any diligence.

(Draft Bill, s 81)

Correcting the register

28.58 Where a statutory pledge has been extinguished as a result of being enforced we consider that the secured creditor should have to apply to the Keeper as soon as reasonably practicable to correct the statutory pledges record to remove the entry.[40] Leaving it in place could prejudice the provider by giving a false impression. Similarly, if a statutory pledge is extinguished as a result of the enforcement of another right in security over the same property, or the execution of diligence against that property, there should be the same duty. For example, A Ltd grants a statutory pledge over its equipment to the Brilliant Bank. A Ltd then grants a second ranking statutory pledge over the same equipment to the Less Brilliant Bank. A Ltd defaults on its secured obligation to the Brilliant Bank and the office equipment is sold, with all the proceeds going to that bank. There is nothing left for the lower ranking Less Brilliant Bank. But, nevertheless, its statutory pledge has been extinguished and it should require to correct the RSP to remove the relevant entry. We recommend:

150. Where a statutory pledge is extinguished as a result of it or another right in security over the same property being enforced, or as a result of diligence being executed against that property, the secured creditor should be required, as soon as reasonably practicable, to apply to the Keeper to correct the Register of Statutory Pledges to remove the relevant entry.

(Draft Bill, s 83)

Liability for loss suffered by virtue of enforcement

28.59 In this chapter we have set out a series of rules in relation to how a pledge may be enforced. Where these rules are transgressed, a party who suffers a loss should be entitled to compensation from the secured creditor on the basis of breach of statutory duty.[41] Some examples may assist.

28.60 Example 1. John owns a house boat. He grants a first statutory pledge over it in favour of Kirk in security of a loan. One year later he grants a second statutory pledge over it in favour of Louise in security of another loan. John defaults on the loans. After obtaining a court order, since John is a private individual, Kirk enforces by selling the house boat. He fails to obtain the price that is the best reasonably obtainable resulting in no proceeds being left for Louise and John. If he had made proper efforts there would have been a surplus which could have paid Louise's debt with some money left to return to John. Both Louise and John have a compensation claim against Kirk for their financial loss.

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[40] On corrections, see Chapter 33 below. Of course there would be no need for a correction where a statutory pledge has been created without registration as a financial collateral arrangement under the FCARs. See Chapter 37 below.

[41] Cf DCFR IX.–7:104; City of London Law Society draft Secured Transactions Code s 50.

28.61 Example 2. Same as example 1, but there are free proceeds to pay Louise and some money to return to John. Kirk fails to pay them. They have a compensation claim against Kirk in respect of what is due to them.

28.62 Example 3. Same as example 1, but this time Kirk fails to obtain a court order and unlawfully evicts John and members of his family who are living in the house boat. They have a compensation claim in respect of the loss suffered by them, for example, the cost of finding alternative accommodation.

28.63 We think that the entitlement to compensation should be subject to the general legal doctrines that a party making a claim has a duty to mitigate loss and that claims for losses which are not reasonably foreseeable should be disallowed.[42] For example, in relation to mitigation, if the provider is aware that the secured creditor is about to sell the property in a manner which would not achieve the price that is the best reasonably obtainable they should seek to prevent this from happening. In contrast with other liability provisions which we recommend,[43] we consider that claims in respect of non-patrimonial loss (*solatium*) should *not* be excluded. In Example 3 above, John and his family may have been caused stress by the unlawful eviction.

28.64 We recommend:

151. (a) A person should be entitled to be compensated by a secured creditor for loss suffered in consequence of the secured creditor's failure to comply with the statutory obligations imposed on the secured creditor in relation to enforcement.

(b) But the secured creditor should have no liability:

(i) in so far as the loss could have been avoided by the person taking certain measures which it would have been reasonable for the person to take, and

(ii) in so far as the loss is not reasonably foreseeable.

(Draft Bill, s 85)

Service of documents

28.65 As has been seen, some parts of the enforcement procedure would involve the service of documents by the secured creditor on the provider, notably the Pledge Enforcement Notice. Section 26 of the Interpretation and Legislative Reform (Scotland) Act 2010 sets out rules on service which apply to Acts of the Scottish Parliament except where contrary provision is made.[44] In essence, service can be made (a) personally; (b) by post; and (c) electronically, subject to certain conditions.[45] Section 26 also contains a definition of

[42] We have drawn here on the Land Registration etc. (Scotland) Act 2012 ss 94 and 106.
[43] See paras 11.22–11.42 above and paras 35.33–35.36 below.
[44] We refer to this provision elsewhere in this Report. See paras 5.48–5.57 above.
[45] Interpretation and Legislative Reform (Scotland) Act 2010 s 26(2).

a person's "proper address", at which service is to be made.[46] For example, in the case of a body corporate it is the address of the registered or principal office of the body.

28.66 We think that the secured creditor and provider should be able to agree that enforcement documents are to be served by only one of the specified methods, for example, electronically. In addition it should be possible for them to agree an address, other than the "proper address" as defined in section 26, as the place where service is to be made. We think that such an agreement should require to be made in writing. If, however, the agreement is made and it is impossible for service to be effected in terms of it, the agreement should be disregarded and service permitted in terms of section 26. For example, if a particular postal address is provided, but the provider is found no longer to be at that address, service can be effected at that person's "proper address".

28.67 We recommend:

152. (a) In respect of the application of section 26 of the Interpretation and Legislative Reform (Scotland) Act 2010 in relation to the service of enforcement notices the provider and the secured creditor should be able to agree that service is to be effected either or both at a specified address and by a specified method.

(b) Such an agreement should require to be in writing.

(c) Where there is such an agreement but service cannot be effected in accordance with it the agreement is to be disregarded.

(Draft Bill, s 86)

[46] 2010 Act s 26(4).

Chapter 29 Register of Statutory Pledges: introduction

Introduction

29.1 In this chapter we consider the setting-up, management and nature of the new Register of Statutory Pledges (RSP). We draw here on a number of our earlier recommendations in relation to the Register of Assignations (RoA).

Establishment of the RSP

29.2 In the Discussion Paper we set out our view that registration in a new register should be (i) an optional alternative to intimation as a method of transferring claims; and (ii) the method by which statutory pledges would be created.[1] Elsewhere in this Report, following support from consultees, we have now taken forward these suggestions as recommendations.[2]

29.3 The Discussion Paper proposed that a new public register should be established, provisionally to be called the Register of Moveable Transactions, in which (i) assignations of personal rights and (ii) securities over moveable property (corporeal and incorporeal) could be registered. This proposal was supported by consultees.

29.4 As we explained earlier,[3] when we came to work on the draft legislative provisions which would establish the new register it became apparent that the assignation and statutory pledge parts would be significantly different. We reached the view that it would be preferable to have two separate registers.

29.5 We therefore recommend:

153. A new public register should be established, to be called the Register of Statutory Pledges, in which statutory pledges can be registered.

(Draft Bill, s 87(1))

Management of the RSP

29.6 There are two main possibilities for the management of the RSP. The first is Companies House. The Murray Report proposed that the new "moveable security" which it recommended should be registrable in the Companies Register.[4] But, as we noted in the Discussion Paper,[5] there was a certain awkwardness with this as the security right could be granted by persons other than companies. This is true also of the statutory pledge.

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[1] Discussion Paper, para 20.1.
[2] See paras 5.1–5.22 and 23.11–23.19 above. But registration would not be required in respect of statutory pledges over financial instruments. See Chapter 37 below.
[3] See paras 6.4–6.6 above.
[4] Murray Report, para 3.11.
[5] Discussion Paper, para 20.2.

Furthermore, unlike the Murray Report security, it would be available to consumers (subject to certain restrictions). A further issue with using Companies House is that it reports to the Department for Business, Energy and Industrial Strategy rather than the Scottish Government. In this Report our objective is to present a set of recommendations that can for the most part be implemented using devolved powers.

29.7 The second candidate is Registers of Scotland. We have already recommended that it should be responsible for the new RoA.[6] The RSP would be its sister register. It clearly makes sense for Registers of Scotland to be responsible for this register too. Registers of Scotland agree.

29.8 We therefore recommend:

154. The register should be under the management and control of the Keeper of the Registers of Scotland.

(Draft Bill, s 87(2))

Merger with the Register of Floating Charges

29.9 In the Discussion Paper we asked whether the new register should be merged with the Register of Floating Charges provided for by Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007.[7] But, as discussed above,[8] Part 2 has never been brought into force. This question is therefore effectively superseded.

Costs

29.10 The costs implications in relation to RSP are equivalent to those for the RoA and we refer to our earlier discussion of this subject.[9]

The RoA and RSP compared

29.11 Like the RoA, the RSP would not be a title register in relation to moveable property.[10] It would only be a register of statutory pledges. The fact that Yuliya has granted a statutory pledge over her motor vehicle in favour of Zara and that this grant has been registered in the RSP would not amount to confirmation that Yuliya owns the vehicle.

29.12 That said, the RSP would be markedly different from the RoA in that the RoA would be a register of assignation documents. As discussed earlier in the Report, an assignation differs materially from a statutory pledge in that the former is a transfer whereas the latter is a right.[11] The RSP therefore cannot be a mere register of constitutive documents of statutory pledges. It requires to take account of other juridical acts in relation to a statutory pledge, in particular amendment, assignation, restriction and discharge. Therefore in contrast to the RoA where an entry would be for the assignation document, the entry in the RSP would be for the statutory pledge and it would be possible to amend the registration in accordance

[6] See paras 6.8–6.10 above.
[7] Discussion Paper, para 20.3.
[8] See paras 18.23–18.25 above.
[9] See para 6.11 above.
[10] See para 6.12 above.
[11] See para 1.35 above.

with the recommendations set out in Chapter 23 above[12] or correct the entry in accordance with the recommendations set out in Chapter 33 below.

What is to be registered?

Constitutive documents

29.13 Earlier in this Report in relation to assignations we discussed at length the relevant merits of (i) notice filing and (ii) transaction filing, by means of registering the assignation/security document.[13] We concluded in favour of the latter. The arguments are little different for the constitutive document of a statutory pledge and indeed document registration is familiar for grants of existing security rights by companies under Part 25 of the Companies Act 2006.[14] Document registration was overwhelmingly supported by consultees and our advisory group.

29.14 We recommend:

> **155. Where an application is made for registration of a statutory pledge it should require to be accompanied by a copy of the constitutive document.**
>
> (Draft Bill, s 91(2)(a)(ii))

Other documents

29.15 We discussed the various juridical acts in relation to a statutory pledge in Chapter 23 above. We concluded that in the interests of commercial flexibility and reducing costs it should be possible for these generally to be carried out without the need for registration (and thus the need for registration of the relevant document). But for amendments extending the scope of the encumbered property or secured obligation we recommended registration because of the impact on third parties.

29.16 A "registration-light" approach is the broad position under UCC–9 and the PPSAs, where there is notice filing. In contrast, registration is normally required with standard securities,[15] but this is in the context of an asset-based register and land transactions being more registration-based than moveable transactions. For example, the transfer of land requires registration whereas the transfer of a corporeal moveable does not. The position as regards floating charges is patchy. The instrument itself and any amendment ("instrument of alteration") require to be registered.[16] An assignation of a floating charge cannot be registered. Instruments altering ranking may be registered.[17] A restriction ("release") or discharge ("satisfaction") may be registered. But in these cases rather than a document only a "statement" and "particulars" must be delivered to the register.[18]

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[12] See paras 23.33–23.56 above.
[13] See paras 6.13–6.30 above.
[14] See Chapter 36 below.
[15] Conveyancing and Feudal Reform (Scotland) Act 1970 ss 14–17.
[16] Companies Act 2006 s 859A(3); Companies Act 1985 s 466(4B).
[17] Companies Act 2006 s 859O(2)(a).
[18] Companies Act 2006 s 859L.

29.17 We have considered this matter carefully. The more documents that appear on the register the more cluttered it becomes and the more difficult to search. We have concluded, however, that amendments which add further property to the encumbered property or which increase the secured obligation should require registration of the relevant document.

29.18 If there is a requirement to register the constitutive document which describes the initial encumbered property, then it would seem to follow logically that any document adding property should also be registered. Third parties consulting the register need to be able to see the amended description of the encumbered property. While this policy could be achieved by means of registering a statement, the same could be said in relation to the original description and, as we saw above, our advisory group favoured document registration. Requiring registration of the amendment document also provides a measure of debtor protection. Of course there is always the possibility of forgery, but this is likely to be rare.

29.19 Similar arguments apply to increasing the extent of the secured obligation. An amendment which changes the secured debt from say £10,000 to all sums due and to become due makes the statutory pledge more powerful and is of material interest to prospective secured creditors. In practice, security documentation often defines the secured obligation from the outset as being all sums due or to become due. Alternatively it defines it by reference to off-register documents. As discussed earlier,[19] here there would seem to be no point in having to update the entry if these documents are amended because the scope of the secured obligation cannot be directly seen from the register in any event. We therefore think that registered amendments of the secured obligation would be rare.

29.20 For the juridical acts of assignation, restriction or discharge it is worth reiterating that registration would not be necessary or indeed possible. As discussed in Chapter 23 above,[20] these acts would take place off-register, but the relevant entry in the register could be altered or deleted to reflect the up-to-date legal position by means of an application for correction.[21] We do not think that the correction should be required to be accompanied by a document giving effect to the juridical act. This would clutter the register.

29.21 We recommend:

156. A copy of a document amending a registered statutory pledge to add property to the encumbered property or to increase the extent of the secured obligation should require to be registered.

(Draft Bill, s 92(2)(b))

Form and protection of the RSP

29.22 As with the RoA we think that the Keeper should keep the RSP in electronic form, although the exact detail should be a matter for her.[22] In the interests of flexibility, once again, we do not formally recommend that the register must be held electronically.

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[19] See para 23.35 above.
[20] See paras 23.49–23.56 above.
[21] See Chapter 33 below.
[22] See para 6.31 above.

29.23 In line with the position for the Land Register and the RoA,[23] we consider that the Keeper should be under a duty to take such steps as appear reasonable to her to protect the RSP from interference, unlawful access or damage. We recommend:

157. (a) Subject to the requirements of statute, the register should be in such form as the Keeper thinks fit.

(b) The Keeper should take such steps as appear reasonable to her for protecting the register from interference, unauthorised access, or damage.

(Draft Bill, s 87(3) & (4))

Form of registration

29.24 For the reasons discussed above in relation to the RoA we think that registration in the RSP should be online only and automated. The application would not be checked by the Keeper.[24]

158. Registration in the RSP should be by electronic means only and should be by means of an automated system under which applications are not checked by the Keeper.

(Draft Bill, s 119)

[23] Land Registration etc. (Scotland) Act 2012 s 1(5).
[24] See paras 6.33–6.45 above.

Chapter 30 Register of Statutory Pledges: structure, content and applications for registration

Introduction

30.1 In this chapter we consider the structure of the RSP, the data and documents which should be registered and the application process for registration.

Structure of the RSP

30.2 The main part of the RSP would be the statutory pledges record. As for the Land Register and the RoA,[1] we consider that there should also be an archive record, in which archived material is kept by the Keeper. The archive record in the RSP would have a more significant role than its counterpart in the RoA, because it would be the home for discharged statutory pledges where the RSP is corrected to reflect the discharge. We consider archiving further later,[2] but for the moment we recommend:

> **159. The Keeper should make up and maintain, as parts of the Register of Statutory Pledges:**
>
> **(a) the statutory pledges record, and**
>
> **(b) the archive record.**
>
> (Draft Bill, s 88)

Information appearing in the RSP: general

30.3 As for the RoA, we think that an entry in the register should contain key data, such as the details of the provider and secured creditor, rather than merely hold the constitutive document of the statutory pledge.[3] Our draft Bill makes provision for the information that is to appear in an entry. It also confers power on the Scottish Ministers to make rules (known as RSP Rules)[4] providing for more detailed requirements.

Statutory pledges record

30.4 We think that the statutory pledges record should contain similar data to that in the assignations record in the RoA.[5] Of course rather than the details of the assignor and assignee there would be details of the provider and the secured creditor. And rather than a copy of the assignation document there would be a copy of the constitutive document of the

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[1] Land Registration etc. (Scotland) Act 2012 s 14. On the RoA see para 7.2 above.
[2] See paras 35.30–35.32 below.
[3] See para 7.3 above.
[4] See paras 35.37–35.38 below.
[5] See paras 7.3–7.27 above.

statutory pledge. There would also be a copy of any amendment document adding property to the encumbered property or increasing the extent of the secured obligation.

30.5 In the Discussion Paper, we expressed the view that the secured obligation should be stated in the entry.[6] But this is typically not a requirement under UCC–9 and the PPSAs. Nor is it a requirement under the post-1 April 2013 version of Part 25 of the Companies Act 2006.[7] The DCFR Book IX allows for the maximum amount of the security to be registered.[8] The UNCITRAL Model Law on Secured Transactions gives countries the option of requiring registration of a statement of the maximum amount for which the security right may be registered.[9] In line with these comparators, we have now concluded that the secured obligation should not be required data in the entry. Our thinking is as follows. It would be possible to see the secured obligation in the constitutive document which would appear in the entry. We expect that this would often be for all sums due and to become due. It should also be possible to enquire as to the up-to-date position as regards the secured obligation by means of a request for information.[10] Further, the secured obligation is not data which would be suitable as the subject of a search. Any search against "all sums due and to become due" would produce thousands of results.

30.6 The encumbered property would have to be described in the way which any rules required. Similar possibilities arise as for the description of claims described above.[11] As we mentioned, many of the PPSA jurisdictions have asset classes. For example, the classes in New Zealand include "goods: motor vehicles", "goods: livestock", "goods: crops" and "goods: other". An advantage of this is that someone only interested in say livestock can rely on there being no perfected security interest if the livestock category has not been completed on the notice that has been registered.

30.7 Unlike claims whose assignation is registered in the RoA, some encumbered property would have a unique number which could be required to be stated in the entry. The leading example of this is the vehicle identification number (VIN) of motor vehicles. UCC–9 and the PPSAs typically allow, or in some cases require, VINs to be registered.[12] The Canadian PPSAs (other than Ontario and Yukon) also provide for the registration of the serial numbers of trailers, motor homes, aircraft,[13] boats and outboard motors for boats.[14]

30.8 The advantage of using unique numbers is that they can protect remote transferees. Imagine that Jack grants a statutory pledge over his car to the Braemar Bank. He then sells it to Katherine without the permission of the bank. The car remains subject to the statutory pledge. Katherine then sells the car to Louise. But a search in the RSP against Katherine would not reveal the statutory pledge, because it has been registered against Jack and not Katherine. The RSP is primarily a person-based register. But if the VIN for the car were registered Louise would be able to find the statutory pledge by searching against that

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[6] Discussion Paper, para 20.26.
[7] Companies Act 2006 s 859D.
[8] DCFR Book IX.–3:307(c).
[9] UNCITRAL Model Law on Secured Transactions art 8(e).
[10] See paras 35.2–35.19 below.
[11] See paras 7.15–7.22 above.
[12] Under the NZ Personal Property Securities Regulations 2001 sch 1 art 9 it is necessary for the VIN to appear on the financing statement where the motor vehicle is "consumer goods" or "equipment".
[13] Statutory pledges may not be granted over aircraft. See para 21.12 above.
[14] See Cuming, Walsh and Wood, *Personal Property Security Law* 349–351.

number and the good faith acquirer provisions which we recommend later would not be engaged, thus making the pledge more robust.[15]

30.9 Finally, the entry should contain any data otherwise required by legislation, for example, details of corrections.[16]

30.10 We recommend:

160. An entry in the statutory pledges record should comprise:

(a) the provider's name and address,

(b) where the provider is an individual, the provider's date of birth,

(c) any number which the provider bears or other information relating to the provider which, by virtue of RSP Rules, must be included in the entry,

(d) the secured creditor's name and address,

(e) any number which the secured creditor bears or other information relating to the secured creditor which, by virtue of RSP Rules, must be included in the entry,

(f) where the secured creditor is not an individual, an address (which may be an email address) to which requests for information regarding the statutory pledge may be directed,

(g) such description of the encumbered property as may be required or permitted by RSP Rules,

(h) a copy of the constitutive document of the statutory pledge and any amendment document,

(i) the registration number allocated to the entry,

(j) the date and time of registration of the statutory pledge and any amendment to it, and

(k) such other data as may be required by legislation.

(Draft Bill, s 89(1))

Applications for registration: general

30.11 Applications for registration would be made online. The following transactions could be registered in the RSP: (a) a statutory pledge; and (b) an amendment to a statutory pledge adding encumbered property or increasing the extent of the secured obligation. A contrast

[15] For discussion of this issue further in the context of the protection of good faith purchasers, see Chapter 32 below.
[16] On corrections, see Chapter 33 below.

can be noted with the RoA where only an assignation document is registrable. This underlines the previously mentioned distinction between an assignation as a transfer and a statutory pledge as a right.[17]

Application for registration of a statutory pledge

30.12 The applicant would be the secured creditor. But the application could be made by an agent such as a solicitor.

30.13 We think that the Keeper should have to accept the application provided that certain conditions are satisfied. First, it would have to conform to RSP Rules. The rules would set out the form of application and the data fields that would require to be completed.[18] Secondly, a copy of the constitutive document would require to be submitted.[19] Thirdly, the application would require to provide the Keeper with the necessary information to make up an entry for it in the RSP. Fourthly, the applicant would have to pay the relevant fee. If the requirements were not satisfied the Keeper would be bound to reject the application.

30.14 We recommend:

161. (a) An application for registration of a statutory pledge should be made by or on behalf of the secured creditor.

(b) The Keeper should be required to accept an application if:

(i) it conforms to RSP Rules in relation to applications,

(ii) it is submitted with a copy of the constitutive document,

(iii) it provides the Keeper with the necessary data to make up an entry in the RSP, and

(iv) the registration fee is paid or the Keeper is satisfied that it will be.

(c) Where these requirements are not satisfied, the Keeper should be required to reject the application and inform the applicant accordingly.

(Draft Bill, ss 91(1) to (3) and 118(4))

Creation of an entry in the statutory pledges record

30.15 The process for creation of an entry would be very similar to that for the RoA.[20] Provided that the application requirements were met, the Keeper's computer system would make up the entry and allocate a unique number to it.

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[17] See para 6.4 above.
[18] Registration legislation in Scotland and elsewhere typically leaves the details of applications to secondary legislation in the interests of flexibility.
[19] See paras 29.11–29.12 above.
[20] See para 7.30 above.

30.16 We recommend:

162. On accepting an application for registration, the Keeper should be required to:

(a) make up and maintain in the statutory pledges record an entry for the statutory pledge, and

(b) allocate a registration number to the entry.

(Draft Bill, s 91(4))

Applications for registration of an amendment

30.17 The process for registration applications in relation to amendments would be very similar to that for the original registration of the statutory pledge described above. While the details would be for the Keeper to specify when the register is being set up, we envisage a system used in other jurisdictions[21] where, following the initial registration of the statutory pledge, the secured creditor is provided with a PIN number/password which can be used to make changes to the registration.[22] It would be necessary of course to submit a copy of the amendment document.

30.18 We recommend:

163. (a) An application for registration of an amendment of a statutory pledge to add property to the encumbered property or to increase the extent of the secured obligation should be made by or on behalf of the secured creditor.

(b) The Keeper should be required to accept an application if:

(i) it conforms to RSP Rules in relation to applications,

(ii) it is submitted with a copy of the amendment document,

(iii) it provides the Keeper with the necessary data to update the entry in the RSP, and

(iv) the registration fee is paid or the Keeper is satisfied that it will be.

(c) Where these requirements are not satisfied, the Keeper should be required to reject the application and inform the applicant accordingly.

(Draft Bill, ss 92(1) to (3) and 118(4))

[21] Notably New Zealand.
[22] That is to say on the registration of a financing statement, the password/PIN number is issued and must be used to register a financing change statement.

Giving effect to amendment applications

30.19 Where an application for registration of an amendment is accepted, the Keeper's computer system would have to amend the entry. Thus the amendment document would be added to it.

30.20 If a system of asset classes were used, then in the case of an amendment adding a type of property in a different asset class[23] from the original encumbered property the entry would also have to be altered to state the added class.

30.21 We recommend:

> **164. On accepting an application for registration of an amendment the Keeper should be required to update the entry for the statutory pledge accordingly.**
>
> (Draft Bill, s 92(4))

Verification statements

30.22 As with the RoA, we think that the Keeper's computer system should send the applicant a verification statement which confirms that the application has been successful and that the statutory pledge has been registered. We mentioned earlier the PIN (personal identification number) system used in some jurisdictions which enables the secured creditor to register a financing change statement to amend the entry.[24] The PIN is issued with the verification statement. The RSP might operate using a similar system in relation to statutory pledges where further registrations are possible, to amend the pledge, as well as applications for correction of the entry.[25]

30.23 For the reasons discussed earlier in relation to the RoA we do not recommend a duty on the secured creditor to send a copy of the verification statement to the provider, but we think that the provider should be entitled to request a copy, with the secured creditor having to respond within 21 days.[26] This would enable the provider to check that its contact details were correct so that it would be notified of any correction made by the secured creditor under the automated procedure which we recommend below.[27]

30.24 We recommend:

> **165. (a) The Keeper should be required to issue a verification statement on accepting an application for registration.**
>
> **(b) The statement should require to conform to RSP Rules. It should include the date and time of the registration and the unique number allocated to the entry to which the application relates.**

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[23] See para 30.6 above.
[24] See para 30.17 above. We are grateful to Sheree McDonald, Senior Solicitor in the Ministry of Economic Development in Auckland for her help here.
[25] On corrections, see Chapter 33 below.
[26] See paras 7.33–7.40 above.
[27] See paras 33.11–33.22 below.

(c) The provider should be entitled to request a copy of the verification statement and the secured creditor should be required to supply this within 21 days after the request is made.

(Draft Bill, s 93)

Date and time of registration

30.25 As with the RoA,[28] the date and time of a registration would be of high importance for priority purposes as regards statutory pledges. The Keeper's computer system would determine when the relevant entry is made up or amended. The relevant date and time would then be stated in the entry. The registration in respect of which the application reaches the Keeper first should have priority.[29] The computer system should be able to ascertain which application that is. We recommend:

166. (a) A registration should be taken to be made on the date and time which are entered for it in the Register of Statutory Pledges.

(b) The Keeper should be required to deal with applications for registration and allocate these registration numbers in order of receipt.

(Draft Bill, s 94)

[28] See paras 7.41–7.42 above.
[29] See LR(S)A 2012 s 39(1).

Chapter 31 Register of Statutory Pledges: effective registration

Introduction

31.1 This chapter considers effective registration in the statutory pledges record. Our thinking here is very similar to that in relation to effective registration in the assignations record, which we discussed in Chapter 8 above. Here we can therefore be briefer. The central ideas are that the entry in the register should be capable of being found and provide a copy of the constitutive document (and any amendment document) which can be inspected by the searcher.

Effective registration of statutory pledge

31.2 As for assignations, a registration would fail to be effective in the following two circumstances.

(1) Entry does not include a copy of the constitutive document or document is invalid

31.3 If the correct constitutive document does not appear in the relevant entry in the statutory pledges record or that document is invalid the registration should be ineffective.[1]

(2) Entry contains an inaccuracy which is seriously misleading

31.4 If the data in the entry contains an inaccuracy which is seriously misleading at the time of the registration the registration should be ineffective. Below, we consider the "seriously misleading" test in more detail, but before that we recommend:

> **167. The registration of a statutory pledge should be ineffective if the entry made up for it:**
>
> **(a) does not include a copy of the constitutive document,**
>
> **(b) that document is invalid, or**
>
> **(c) there is an inaccuracy in relation to the data registered which, as at the time of registration, is seriously misleading.**
>
> (Draft Bill, s 95(1))

Effective registration of amendment to statutory pledge

31.5 Similar rules would apply in relation to amendments of statutory pledges. First, a copy of the correct amendment document should require to appear in the register entry or the registration of the amendment would be ineffective. Secondly, the document should

[1] See also para 8.4 above.

require to be valid. Thirdly, the entry as amended should not contain an inaccuracy in relation to the data in it which, in consequence of the amendment, is seriously misleading. For example, Jill grants Keith an amendment document extending the statutory pledge over her vehicle to include a patent which she holds. In registering this Keith fails to comply with RSP Rules and fails to tick the box for "intellectual property" on the application. This could be subsequently put right by means of a correction.[2]

31.6 We recommend:

> **168. The registration of an amendment to a statutory pledge should be ineffective if:**
>
> **(a) the entry for the statutory pledge does not include a copy of the amendment document,**
>
> **(b) that document is invalid, or**
>
> **(c) there is an inaccuracy in relation to the data registered for the statutory pledge in consequence of the amendment which is seriously misleading.**
>
> (Draft Bill, s 96(1))

Seriously misleading inaccuracies in entries in the statutory pledges record

Introduction

31.7 Similar detailed rules should apply as for the assignations record in the RoA.[3] But, in contrast to the position there, where the "seriously misleading" test would only be relevant to the details at the time the assignation document was registered, in the RSP the test would also play a key role in the question of supervening inaccuracies. These are the subject matter of the next chapter.

(1) An objective test

31.8 The "seriously misleading" test would be an objective one.

(2) No account should be taken of statutory pledge documents

31.9 Determining where an inaccuracy is seriously misleading should not take any account of the constitutive document or any amendment document.

(3) Registration ineffective in part

31.10 Some inaccuracies would only make the registration ineffective in part. Example 1. Hannah grants a statutory pledge over her Porsche and patent to Jasmine. Jasmine registers the statutory pledge in the RSP but only ticks the box in the application form for vehicles and not the one for intellectual property. The registration should be ineffective as regards the patent. Example 2. Ben and Catherine own a car. They grant a statutory

[2] See Chapter 33 below.
[3] See paras 8.16–8.30 above.

pledge over it to Diane. She registers the statutory pledge in the RSP, but when completing the application for registration states that Ben is the provider but fails to mention Catherine. The registration is only effective as regards Ben's share of the car. Example 3. Sally grants a statutory pledge over her patent to Tom and Una. Tom (with Una's consent) registers the statutory pledge in the RSP, but when completing the application form for registration by mistake only states that Tom is the secured creditor. The registration is only effective as regards the share of the pledge granted to Tom.

(4) Specific cases where search does not retrieve entry

31.11 We recommend similar rules as for assignation, but with an additional one for property with a unique number.

31.12 The first rule would apply where the provider is a person required by RSP Rules to be identified in the entry by a unique number. If a search against that number did not retrieve the entry the registration should be ineffective because of this seriously misleading inaccuracy. In contrast a wrongly-stated name for such a person would not be fatal.

31.13 The second rule would apply where the provider was not required by RSP Rules to be identified in the entry by a unique number. If a search against the provider's "proper name" did not retrieve the entry the registration should be ineffective.

31.14 The third rule would apply to providers who were individuals. If a search against the provider's "proper name" and date of birth did not retrieve the entry the registration should be ineffective.

31.15 The fourth and additional rule would relate to property with a unique number. The classic example is VINs (Vehicle Identification Numbers). In some circumstances, the PPSAs require a VIN to be registered. The advantage of this is that it is possible to search against the vehicle, no matter whose possession it is in. For example, in New Zealand where the motor vehicle in question is "consumer goods, or equipment" there are requirements to register the registration number (plate number), VIN and, if there is no VIN, but there is a chassis number, that number.[4] A similar approach could be taken under RSP Rules. One controversial issue in some PPSA jurisdictions is whether a registration is ineffective where although the property's unique number is correctly stated there is a seriously misleading error or omission in the debtor's (provider's) details.[5] The better view is that the registration here should be ineffective.[6] This is the view which we take too.[7]

31.16 Once again these rules would have common features. First, the search would be for the provider's details as at the date and time the registration was made. It is at that point that the details have to be correct. In Chapter 32 we deal with the consequences of these details changing later, for example if the provider changes name. Secondly, the search would be by means of a specific type of search facility which the Keeper would provide.

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[4] NZ PPSA 1999 s 150(b) and Personal Property Securities Regulations 2001 Sch 1 art 9. See Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 474–476.

[5] Compare *Kelln (Trustee of) v Strasbourg Credit Union Ltd* (1992) 89 DLR (4th) 427, 3 PPSAC (2d) 44 (Sask CA) and *Re Lambert* (1994) 119 DLR (4th) 93; 7 PPSAC (2d) 240 (Ont Ca).

[6] See Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 477–478 and Cuming, Walsh and Wood, *Personal Property Security Law* 367–368.

[7] But we recommend a different rule where the provider's name is originally registered correctly, but there is a supervening inaccuracy as to that name. See para 32.50 below.

(5) Power to specify further instances in which an inaccuracy is seriously misleading

31.17 As for assignations, we think that the Scottish Ministers should have a power to specify other circumstances in which an inaccuracy would be seriously misleading.

31.18 We recommend:

169. (a) An inaccuracy in an entry in the statutory pledges record may be seriously misleading irrespective of whether any person has been misled.

(b) In determining whether an inaccuracy is seriously misleading no account should be taken of any document included in the entry.

(c) An inaccuracy which is seriously misleading in respect of part of an entry should not affect the rest of the entry.

(d) Without prejudice to the generality, an inaccuracy should be seriously misleading:

(i) where the provider (or as the case may be, a co-provider) is not a person required by RSP Rules to be identified by a unique number, if a search using a designated facility provided for by the Keeper for:

(a) the provider's (or co-provider's) proper name, or

(b) the provider's (or co-provider's) proper name and the provider's (or co-provider's) date of birth

does not disclose the entry,

(ii) where the provider (or, as the case may be, co-provider) is a person required by RSP Rules to be identified by a unique number, if a search using a designated facility provided for by the Keeper for that number does not disclose the entry, including where a search using such a facility for the provider's (or co-provider's) number does disclose the entry,

(iii) in respect of so much of the encumbered property as bears a unique number which must, by virtue of RSP Rules, be included in the statutory pledges record, if a search using a designated facility provided for by the Keeper for that number does not disclose the entry.

(e) The meaning of "proper name" should be set out in RSP Rules.

(f) The Scottish Ministers should be able to specify further instances in which an inaccuracy is seriously misleading.

(Draft Bill, s 98)

Chapter 32 The Register of Statutory Pledges: supervening inaccuracies and the protection of third parties

Introduction

32.1 In the previous chapter we set out recommendations on what would be required for an effective registration in the Register of Statutory Pledges. In broad terms the secured creditor who is registering would require to ensure that the details which were entered into the application for registration and which would form the basis of the entry are correct. In particular, there would require to be no seriously misleading inaccuracies.

32.2 In contrast to an entry in the Register of Assignations which would relate to an assignation document, an entry in the RSP would relate to a right – the statutory pledge. The accuracy of that entry could be affected by subsequent events affecting that right. As a result, the entry would misstate what the position is in fact or law in relation to the statutory pledge. This inaccuracy might well be seriously misleading. In particular, there would be a risk of "false negatives" in that a search fails to disclose a subsisting statutory pledge due to the fact that the the provider's details have changed since the original registration.

32.3 The question of supervening inaccuracies involves a classic property law dilemma: having to choose between two innocent parties. Here these are (1) the secured creditor who is unaware of the inaccuracy and (2) the third party who acquires a right in property unaware that it is encumbered by a statutory pledge. There is no objectively correct answer. Policy choices have to be made.[1]

Types of supervening inaccuracy

General

32.4 The principal types of supervening inaccuracy which are of concern relate to the identity of the provider. This is because the RSP would primarily be a person-based register. Searches would therefore normally be made against the provider.

Provider changes name

32.5 An example best explains the issue. Imagine that Anna Smith grants a statutory pledge over her grand piano in favour of the Berlin Bank. The bank registers the security in the RSP. Anna subsequently marries and changes her name to Anna Taylor. She does not tell the bank. Without obtaining the bank's permission, she sells the piano for £5,000 to

[1] The classic modern statutory example in Scotland is the Land Registration etc. (Scotland) Act 2012 s 86. For discussion in the context of the Canadian PPSAs, see Cuming, Walsh and Wood, *Personal Property Security Law* 356–359.

Colin Davies. He searches against "Anna Taylor" in the RSP and finds nothing. A variation of this example is that rather than buying the piano Colin obtains a statutory pledge over it, not knowing that there is a subsisting pledge in favour of the bank.

32.6 Both the bank and Colin are innocent. On the other hand Anna, by dealing with the piano without obtaining the bank's consent, is blameworthy. The entry in the register is inaccurate because Anna's name has changed. But in the absence of a special rule on supervening inaccuracies the bank's statutory pledge would continue to encumber the property as a fixed security and real right.

Provider transfers the encumbered property

32.7 Again an example helps explains the issue. We can begin with the same facts as above. Anna grants a statutory pledge over her grand piano in favour of the bank. But this time she does not change her name. She sells the piano to Colin for £5,000 without the bank's permission. If Colin had troubled to search the RSP he would have discovered the statutory pledge. He does not bother. He swiftly resells the piano to Denise O'Neill.[2] She carries out a search in the RSP against Colin and finds nothing because the statutory pledge is registered against Anna and not Colin. Once again a variation of this example is Denise obtaining her own statutory pledge over the piano rather than acquiring ownership of the instrument.

32.8 As a result of the transfer from Anna to Colin, Colin becomes the provider of the statutory pledge as successor owner of the piano.[3] At the time of Denise's acquisition the register entry is thus inaccurate. But in the absence of a special rule the bank's statutory pledge would continue to encumber the property and Denise, despite being in good faith and having checked the RSP would suffer prejudice.

Secured creditor changes name or transfers the statutory pledge

32.9 We do not recommend a search facility directly against the secured creditor's name.[4] Thus the impact of the creditor changing its name or transferring the statutory pledge is less severe.

32.10 If the secured creditor does change name (say due to corporate reorganisation) the secured creditor would obviously know about this and could in principle contact the Keeper to update the entry by means of a correction.[5] In contrast, the provider may change identity as described above without the secured creditor knowing about it. But we do not consider in any event that there should be a general rule that secured creditors are obliged to update their details. This would be costly and time consuming, and is of course not the position for

[2] This situation has been described as the "A-B-C-D problem". See R C C Cuming, "Double-Debtor A-B-C-D Problems in Personal Property Security Legislation" (1992) 7 Banking & Finance Law Review 359. See also R Gengatharen, "Double-debtor problems and the PPSA priority rules" 2012 Journal of International Banking Law and Regulation 469.
[3] Even although he did not provide the statutory pledge in the sense of granting it.
[4] See para 34.3 below.
[5] It may be possible for the Keeper to devise a system whereby all entries for a particular secured creditor can be updated at the same time.

standard securities and floating charges.[6] Indeed earlier we recommended that a statutory pledge should be assignable without registration.[7]

32.11 The main prejudice to a third party by reason of a change of secured provider name or identity which resulted in an inaccuracy in the register would be where this prevented an information request in relation to a statutory pledge being answered. We deal with information duties of secured creditors in Chapter 35 below. As regards change of identity, where there has been an assignation the secured creditor identified in the entry would be obliged to provide the requester with the details of the assignee so there should be no prejudice there. As regards change of name, in the case of an incorporated secured creditor the registration number would not have changed nor indeed probably the address. An information request would still probably be able to reach the secured creditor. It is only in cases of non-corporate secured creditors changing name and address that there could be prejudice because of the ensuing difficulty in trying to contact the creditor. In such cases the secured creditor would be best advised to correct the entry.

Some mitigations

32.12 Before considering whether there should be special rules protecting acquirers where the RSP has a supervening inaccuracy, it must be mentioned that some of the recommendations made elsewhere in this Report would provide mitigation.

32.13 In Chapter 24 above we recommended a number of rules protecting good faith acquirers. Thus, for example, if the encumbered property is acquired in good faith from a seller in the ordinary course of a business, or has a value below a prescribed amount and is acquired in good faith wholly or mainly for personal, domestic or household purposes, the acquirer would take free of the statutory pledge.

32.14 Further, in Chapter 31 above we recommended a "seriously misleading" test in relation to effective registration. But for prescribed persons with unique numbers we were of the view that it should be a mistake in that number as stated in the entry which would jeopardise effectiveness and not an error as to name. We had in mind persons such as companies and LLPs which have registration numbers. Therefore, although the RSP would contain a supervening inaccuracy because a company's name had changed, the relevant entry would remain discoverable by searching against the company's number.

32.15 There are some further points on change of name. First, in the original example given above it was not Anna's change of name in itself which was the problem. It is entirely blameless to marry. The problem was caused by her selling the piano without the bank's consent.[8] Supervening inaccuracies are not an issue where the provider behaves and seeks the bank's permission to any dealing with the encumbered property. We expect that most providers would so behave. But inevitably some would not.

32.16 Secondly, the way in which a provider is to be correctly identified for the purposes of the RSP, that is to say the definition of the "proper name" of the provider, would be a matter

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[6] Admittedly, standard securities are normally found by a search against the relevant land and not against the provider.

[7] See paras 23.41–23.48 above.

[8] Since the statutory pledge is a fixed security and real right the effect of transfer without the creditor's consent is that the property continues to be encumbered.

for secondary legislation following consultation. We discuss this subject above.[9] Clearly marriage is the commonest reason for change of name and a woman conventionally takes her husband's name. If a person's name as per that person's birth certificate was chosen as the "proper name" this would remove the difficulty of such name changes. But there are counter-arguments. For example, documentation such as driving licences tends to be more readily to hand.

Four approaches

32.17 There are broadly four ways of approaching the difficulty of supervening inaccuracies in the RSP.

(1) Ignore the inaccuracy

32.18 Under this approach a statutory pledge is unaffected by the inaccuracy. In the examples above the bank would retain its priority despite its security right being undiscoverable. Broadly speaking this is the approach of UCC–9.[10] It can be argued that subsequent acquirers can protect themselves by making enquiries into the history of the asset and the seller.[11] Colin could ask Anna if she has ever changed her name. Denise could ask Colin how long he has owned the piano and from whom he purchased it. But of course the reply may not be accurate. This approach is therefore generous to the secured creditor.

(2) Extinguish the statutory pledge when the entry becomes inaccurate

32.19 The effect of the entry becoming inaccurate is that the statutory pledge is extinguished. In its pure form this approach is patently unsupportable. There may be no subsequent acquirer of a right in the encumbered property who is prejudiced by the inaccuracy. Moreover, a windfall benefit would be conferred on the provider's unsecured creditors. Extinguishing the statutory pledge in such circumstances cannot be justified.

32.20 Many of the PPSAs, however, effectively take this approach but only in a modified way. Where the details of the provider change and the secured creditor becomes aware of this a grace period starts to run during which the register must be corrected.[12] If it is not, then on the expiry of the period the registration becomes ineffective against third parties subsequently acquiring rights in the asset. As between the secured creditor and the third party relying on the register this approach strongly favours the former because the grace period does not start to run until they have knowledge of the inaccuracy. This seems fair in the case of an authorised transfer. But where the transfer is unauthorised the secured creditor is unlikely to know about it. The Australian PPSA, in contrast, takes an approach which more favours the good faith acquirer. Where there is an unauthorised transfer the

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[9] See paras 7.5–7.6 and 30.3 above.
[10] See UCC § 9–507. And see also UNCITRAL Model Law on Secured Transactions Model Registry Provisions art 26 option C.
[11] Compare Cuming, "Double-Debtor A-B-C-D Problems in Personal Property Security Legislation" at 375.
[12] For New Zealand see the NZ PPSA 1999 ss 87–92. For the Canadian PPSA provisions see Cuming, Walsh and Wood, *Personal Property Security Law* 356–359. Under the Ontario PPSA 1990 failure to correct during the grace period leads to the security interest being wholly unperfected, but under the other Canadian PPSAs the result is for the interest to be unperfected as regards interests acquired in the encumbered property after the commencement of the grace period. See also the UNCITRAL Model Law on Secured Transactions Model Registry Provisions arts 25 and 26.

security interest remains temporarily perfected for a grace period.[13] But a good faith purchaser will normally take the property free of the security interest.[14] In contrast where the provider changes name a good faith purchaser is not protected until the grace period expires.[15]

(3) Extinguish the statutory pledge when a right in the property is acquired by a good faith third party

32.21 Under this approach the statutory pledge survives a supervening inaccuracy but is extinguished when a good faith third party acquires a right in the property. Such a party is favoured over the secured creditor. The approach applies to the acquisition of any property right in the asset and thus to new security rights as well as ownership.

(4) Extinguish the statutory pledge when the property is acquired by a good faith third party but only alter its ranking against a subsequently acquired security right

32.22 This approach is similar to (3) although more subtle and thus more complex as regards subsequent security rights acquired in good faith. Acquirers of such security rights are protected as against the statutory pledge affected by the supervening inaccuracy by means of an entitlement to rank as if it did not exist. But the statutory pledge remains valid against others, in particular those who acquired rights between the creation of the statutory pledge and the entry in the register becoming inaccurate.

32.23 The difference between approaches (3) and (4) can be demonstrated by means of an example. Imagine that Alison grants a statutory pledge over her piano to Bank X which registers the pledge in the RSP. She then grants a second statutory pledge over the piano to Bank Y which registers the pledge in the RSP. Alison changes her name to Anne. She subsequently grants a third statutory pledge over the piano to Bank Z. This pledge is also registered. Bank Z is in good faith. Under approach (3) the statutory pledges of Banks X and Y are extinguished by Bank Z's good faith acquisition. Under approach (4) they are not but Bank Z obtains top ranking followed by Bank X and then Bank Y.

32.24 It would appear that this approach is close to that of the DCFR Book IX, at least in the case of an unauthorised transfer. A good faith acquirer of ownership takes free of the security right where the entry in the register is filed against a security provider different from the transferor.[16] And a good faith acquirer of a security right takes free of an existing security right where that party does not know nor can reasonably be expected to know that the security provider has no right to deal with the encumbered asset free of the existing security right.[17] As regards changes of names the DCFR envisages a system whereby providers will

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[13] See Australian PPSA 2009 s 34. The grace period lasts for five business days after the secured creditor acquires knowledge of the transfer. But there is a long-stop of 24 months after the transfer at which time the security becomes unperfected.

[14] Australian PPSA 2009 s 52. This provision has been reviewed as to its fairness between secured creditor and purchaser, with the reviewer recommending that the Australian Government consider the matter as part of any wider review as to whether the Australian PPSA should be amended to follow the Canadian and NZ PPSAs. See Australian Statutory Review 2015 para 7.6.11.

[15] Australian PPSA 2009 s 166 where the grace period again is five business days from the secured creditor acquiring knowledge of the defect with a long-stop of 60 months.

[16] DCFR IX.–6:102(2)(b). And see also DCFR IX.–3:330(2) and IX.–5:303. See Drobnig and Böger, *Proprietary Security in Movable Assets* 690.

[17] DCFR IX.–2:109. See Drobnig and Böger, *Proprietary Security in Movable Assets* 315.

have to accredit with the register and be given a "personal unique identification number"[18] which presumably would stay constant.

A conceptual point

32.25 As discussed earlier, a fundamental aspect of the UCC–9/PPSA approach is the "attachment/perfection" distinction, which does not fit well with property law in Scotland.[19] Where there are grace period provisions and the secured creditor fails to correct the entry timeously, the effect under some of the PPSAs is for the security interest to cease to be perfected.[20] But if the secured creditor subsequently corrects the entry the security interest becomes perfected once more. The security interest in a question with third parties is in effect switched on, switched off and then switched back on again.

32.26 Such an approach once again is a bad fit with our property law. It seems to us more attractive and consistent with principle to address the question of effective registration only at the time that registration is made, but if justified by policy reasons allow good faith acquirers to prevail over a statutory pledge where they are prejudiced by a supervening inaccuracy in the register which means that the statutory pledge cannot be discovered.

Consultation

32.27 In the Discussion Paper we said: "We . . . think that a buyer who has searched the register without discovering the security should take free of it. For example, suppose that W grants a security to X and then sells to Y who later sells to Z. If Z searches the register, the security will not be discovered, since Z will be searching against Y's name. In that case, Z, if in good faith, should be protected."[21] We subsequently asked two questions.[22] The first was whether consultees agreed that a good faith buyer who has used reasonable diligence in searching the register should take free from entries not thereby revealed. The second was whether such a rule should also apply to creditors taking security.

32.28 An overwhelming majority of consultees answered the first question in the affirmative. Most also agreed in relation to the second. ABFA and the WS Society, however, proposed that good faith purchasers should be protected although they have not consulted the register, but that good faith acquirers of security rights should only be protected where they have consulted the register. Dr Hamish Patrick did not favour protecting the acquirers of security rights on the basis that they carry out "other relevant due diligence". Scott Wortley was concerned about priority circles, an issue to which we return below.

Discussion

32.29 Approach (1) favours the secured creditor at the expense of the acquirer who relies on the register. The purpose of requiring registration is publicity. It enables third parties who may be affected by a right to find out about it before transacting. Retaining complete effectiveness irrespective of inaccuracy would render the RSP unreliable for potential

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[18] See Hamwijk, *Publicity in Secured Transactions Law* 350–351.
[19] See para 18.7 above.
[20] For example, the Australian PPSA 2009 s 166 and the Ontario PPSA s 48(3). But under others such as the NZ PPSA 1999 s 90 the acquirer is given priority over the security interest. This is also the approach under the UNCITRAL Model Law on Secured Transactions Model Registry Provisions arts 25 and 26.
[21] Discussion Paper, para 16.42.
[22] Discussion Paper, questions 37 and 38.

acquirers because any asset could be subject to an undiscoverable statutory pledge. We therefore discount approach (1).

32.30 As we have already concluded, approach (2) in its pure form must also be rejected. When subject to a grace period it is more palatable. But the approach taken under the PPSAs strongly favours the secured creditor because the grace period does not start to run until that party has knowledge of the inaccuracy. The acquirer remains unprotected until that point. It seems preferable to give the secured creditor less absolute protection but only to penalise that party when it is necessary in order to protect the reliability of the register. This points to approaches (3) and (4).

32.31 In relation to good faith acquirers of the property, approaches (3) and (4) are identical. The acquirer takes an unencumbered title. The difference is as regards good faith acquirers of security rights. Earlier we gave an example of how the two approaches contrasted.[23] On the basis of that example it seems that approach (4) is more attractive because approach (3) seems to be too blunt an instrument in simply extinguishing the first statutory pledge. Altering its ranking seems much fairer.

32.32 The difficulty, however, is that the example which we gave earlier was a simple one. Approach (4) can in fact lead to complex ranking questions. Take the following example, under which all the statutory pledges relate to the same piano.

32.33 Bank X has a statutory pledge, the entry for which has become inaccurate. Bank Y (who knows about Bank X's pledge) and later Bank Z (who is in good faith) also acquire statutory pledges in the piano. Bank Y, because of its knowledge, was not misled by the inaccuracy and should not therefore be protected by a rule designed to protect those relying on the register. But Bank Z should be. The ranking under approach (4) is therefore as follows. Bank Z ranks above Bank X because of the good faith protection rule. Bank X ranks above Bank Y because Bank Y is in bad faith and the ordinary ranking rule applies, that the earlier created security ranks first. But Bank Y ranks above Bank Z under that ordinary ranking rule. To put it succinctly, Bank Z ranks above Bank X which ranks above Bank Y which ranks above Bank Z. There is a priority circle, the difficulty that Scott Wortley warned against.

32.34 One solution to this is to remove the requirement to be in good faith (notwithstanding that the fairness of doing so can be questioned) and treat all parties as if they know what is discoverable from the register, no more no less. This would mean Y ranking above Z who would rank above X. But even this approach does not remove the potential for priority circles as the following example involving the same piano demonstrates.

32.35 Bank X registers a statutory pledge. The entry in the register becomes inaccurate because the provider changes its name. Bank Y registers a statutory pledge. Bank X then corrects the inaccuracy in the entry for its statutory pledge. The provider changes its name again, leading to an inaccuracy in both entries. Bank X corrects but Bank Y does not. Bank Z registers a statutory pledge. Bank Z ranks above Bank Y because of the protection rule. Bank Y ranks above Bank X once again because of the protection rule. But Bank X ranks above Bank Z because of ordinary ranking as Bank X's security was discoverable from the register when Bank Z obtained its right. Once again there is a priority circle.

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[23] See para 32.23 above.

32.36 Dr John MacLeod, who has assisted us with the registration aspects of the project, has suggested that the priority circle problem under approach (4) can be solved by reference to a more complex ranking tool from the law of inhibitions: Bell's canons of ranking.[24] This would mean Bank X being treated equivalently to a grantee receiving a right in breach of an inhibition and a good faith acquirer as equivalent to an inhibitor. Applying this approach would mean (a) calculating what the secured creditors would obtain on an ordinary distribution (ignoring good faith protection), (b) next calculating what any party entitled to protection would obtain if the statutory pledge against which it is protected was disregarded and (c) then drawing back sums to which the holder of that statutory pledge would be otherwise entitled to make up the difference. Dr MacLeod provided us with a research paper setting out a series of examples. We take the simplest.

32.37 Imagine that the encumbered piano is worth £10,000. Bank X is owed £9,000, Bank Y £8,000 and Bank Z £9,000. They had registered their statutory pledges in that order but Bank X's entry in the register became inaccurate before the other banks registered.

32.38 The ordinary ranking is that Bank X obtains £9,000, Bank Y obtains £1,000 and Bank Z obtains nothing. If Banks Y and Z were in bad faith this ranking would stand. But let us assume that they were in good faith. Both are now entitled to rank as if Bank X's statutory pledge does not exist. This establishes the following "target" sums: Bank Y obtains £8,000 and Bank Z obtains £2,000.

32.39 The second canon of ranking requires "drawback" from the sums due to the holder of the statutory pledge with the inaccurate entry (Bank X). This is then used to top up the allocation due to the other secured creditors towards their target sum. Bank Y, who obtains £1,000 under the ordinary ranking, needs to take £7,000 from Bank X to reach £8,000. Bank Z, who obtains nothing under the ordinary ranking, needs to take £2,000.

32.40 The final ranking is therefore that Bank X obtains nothing,[25] Bank Y obtains £8,000[26] and Bank Z obtains £2,000.[27]

32.41 Variations in timings as well as in good and bad faith on the part of various secured creditors can produce significantly more complicated examples, albeit in practice unlikely to arise. While we agree with Dr MacLeod that this approach can be used to address the difficulty of priority circles, its complexity reduces its attractiveness. In addition this Commission recommended the abolition of Bell's canons of ranking in relation to inhibition specifically because of their complexity.[28] That recommendation was implemented by section 154 of the Bankruptcy and Diligence etc. (Scotland) Act 2007, although as Dr MacLeod has pointed out that provision is not without difficulty.[29]

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[24] Bell, *Commentaries* II, 519.
[25] £9,000 - £7,000 (to Bank Y) - £2,000 (to Bank Z) = 0.
[26] £1,000 + £7,000 (from Bank X) = £8,000.
[27] 0 + £2,000 (from Bank X) = £2,000.
[28] Scottish Law Commission, Report on Diligence (Scot Law Com No 183, 2001) paras 6.39–6.47.
[29] J MacLeod, *Fraud and Voidable Transfer: Scots Law in European Context* (PhD Thesis, University of Edinburgh, 2013) 162–164.

Conclusion on possible approaches

Good faith acquirers of the encumbered property

32.42 We have reached the view that approach (3)[30] should be adopted where a third party acquires the encumbered property when the register entry for a statutory pledge has become inaccurate and has not been corrected.[31] This approach was supported by consultees and most of our advisory group. The rule would only operate where the provider has transferred the encumbered property without the secured creditor's consent. Most providers would not so behave. Banks, however, take account of the fact that a small minority of customers will breach the terms of their security or even commit fraud.

Good faith acquirers of security rights

32.43 We have found this a more difficult matter. Approach (3) is simpler as it avoids ranking issues, in particular priority circles. Approach (4) is more just but it has the potential to be considerably more complicated. A policy choice has to be made. We have concluded in favour of approach (3) given our statutory duty to simplify the law.[32] The result is that the acquisition of a subsequent security right in the encumbered property when the entry for the statutory pledge is seriously misleading would lead to the extinction of the statutory pledge.

32.44 The secured creditor in the statutory pledge would suffer from this approach in two principal situations.[33] The first would be where a subsequent security right is granted following an unauthorised transfer of the encumbered property (whether or not following the provider changing name). As we noted above in relation to good faith acquisition of the encumbered property itself, only a small minority of providers are likely to do this.

32.45 The second would be where the provider changes name and then grants another security right over the property. The change of name in itself is not blameworthy and arguably neither is the second grant of security right as such a grant would not normally prejudice the first creditor under ordinary ranking rules. There may, however, be an express term of the security agreement[34] forbidding subsequent grants. In the absence of that the provider cannot be said to fall into the category of a bank customer who misbehaves. Extinguishing the statutory pledge because of the good faith of the subsequent security holder is perhaps less easy to justify here.

Good faith and reasonable care

32.46 We think that a way of dealing with the issue just highlighted may be to shift the balance slightly towards the holder of the (original) statutory pledge and require the acquirer not only to be in good faith but to exercise reasonable care before it is protected. As to what is reasonable, this would depend on the circumstances. When a bank is offering a secured loan it is standard practice to carry out identity checks including enquiring about previous

[30] Or approach (4) as these are identical in this regard.
[31] On corrections see the next chapter.
[32] Law Commissions Act 1965 s 3(1).
[33] A further possibility is where there is a supervening inaccuracy because the Keeper's computer system fails and deletes data or the entry. But here the Keeper would require to pay compensation. See para 35.34 below.
[34] Generally called a "negative pledge" clause.

names. Indeed there are duties to do so under money laundering legislation.[35] Of course the provider may lie but in asking the question the bank would have exercised reasonable care. Actually having carried out a search in the register and not discovering anything would be further evidence of this standard. It is arguable whether a purchaser should be expected to meet exactly the same standards as a prospective secured creditor. We think that it should depend on the individual facts of the case and would ultimately have to be determined by a court.

Value

32.47 We consider that good faith acquirers should only be protected where they give value. Fairness points to favouring the secured creditor in the statutory pledge over a donee.

Liferents

32.48 Proper liferents[36] over moveable property are now rare, but in principle the same rules protecting subsequent acquirers of security rights in the encumbered property from supervening inaccuracies in a register entry should also apply to acquirers of liferents.

Inaccuracies affecting only part of the property acquired

32.49 Usually a supervening inaccuracy would affect all the encumbered property in which the good faith acquirer obtains a right. This would be the case for example where the provider's name changes or where that property is the subject of an authorised transfer. There might, however, be circumstances where an entry is only inaccurate as regards some of the encumbered property. Imagine that a statutory pledge is created over a vehicle and a patent. Under RSP Rules[37] the application for registration requires that the encumbered property is identified by reference to certain categories, including "vehicles" and "intellectual property". The encumbered property is duly identified but sometime later due to an erroneous correction by the secured creditor[38] or a fault in the Keeper's computer system the entry is changed so that the data field for intellectual property is deleted. A good faith acquirer of the patent should be protected but not of course an acquirer of the vehicle where the entry remains accurate.

Property with unique numbers

32.50 Some moveables, notably motor vehicles, have unique numbers and we recommend elsewhere that it should be possible in prescribed cases for these numbers to appear in a data field in the register entry which can be directly searched.[39] We consider that where this number does appear in the entry the rules protecting acquirers from supervening inaccuracies should not apply because this number would remain constant and the statutory pledge would remain discoverable.

32.51 We recommend:

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[35] See the Proceeds of Crime Act 2002 and the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (SI 2007/692), especially reg 10.
[36] In other words a real right in property entitling the holder to use the property for life.
[37] See paras 35.37–35.38 below.
[38] On corrections see the next chapter.
[39] See para 34.5 below.

170. (a) Where:

(i) a statutory pledge is effectively registered over property,

(ii) at some time after that registration either

(a) the relevant entry in the statutory pledges record comes to contain an inaccuracy which is seriously misleading (whether or not in respect of all the encumbered property), or

(b) is removed from that record, and

(iii) prior to any correction being effected a person acquires, for value and in good faith while exercising reasonable care,

(a) all or part of the encumbered property, or

(b) a right in, or in part of, that property

the statutory pledge should be extinguished, but in the case of an inaccuracy only as regards so much of the property acquired as is property in respect of which the inaccuracy is seriously misleading.

(b) This rule should not apply where there is an inaccuracy in an entry but the property acquired is of a prescribed type and the unique number for the property appears in the entry.

(Draft Bill, s 97)

Chapter 33 Register of Statutory Pledges: corrections

Introduction

33.1 The Register of Statutory Pledges, like the Register of Assignations, would inevitably contain inaccurate data or incorrect documents. A correction mechanism is therefore essential. The scheme which we recommend for the RSP has similarities to that for the RoA which we recommended in Chapter 9 above.

33.2 But, as we have mentioned elsewhere in this Report,[1] different considerations apply to assignations and statutory pledges because the former is a transfer and the latter is a right. Once a transfer has been registered it would be incoherent to be able to "cancel" it by deletion of the relevant entry. Rather, what is required is a re-transfer (retrocession). Therefore we recommended in Chapter 9 that the power to correct the assignations record should be restricted by requiring the involvement of the Keeper. Assignees should not be free to delete an entry ostensibly on the basis that they are "correcting" it.

33.3 In contrast the statutory pledge, as a right, is capable of extinction or being the subject of other juridical acts which render the register inaccurate because these take place off-register. Thus the secured creditor may have discharged the pledge by means of a written statement[2] or consented to the encumbered property being transferred to a third party unencumbered by the pledge.[3] In such circumstances the secured creditor should be able freely to correct the record so that it reflects the true legal position and remove the entry. We recommend below also that there should be a system modelled on the "change demand" procedure in comparator legislation. This would enable another party with an interest, typically the provider, to require the secured creditor to make a correction.

Types of correction

33.4 As for the RoA, five main types of correction may be identified. First, data in an entry could be removed. For example, the entry might state that Alice and Brad are co-providers of a statutory pledge, whereas in truth Alice is the sole provider. Brad's details could be removed by means of a correction. Secondly, an entry could be removed from the statutory pledges record to the archive record. This might happen after a statutory pledge has been set aside by the court. Thirdly, data or a copy document in an entry might be replaced. For example, an error in the Keeper's computer system leads to Kirsten being entered as the provider in an entry whereas it should be Jane. Fourthly, data or a copy document could be restored, for example where it has been erroneously deleted by the Keeper's computer system. Fifthly, an entry could be restored, for example, where the Keeper's computer system has deleted it by mistake.

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[1] See eg para 1.35 above.
[2] See paras 23.49–23.54 above.
[3] See paras 20.37–20.45 above.

33.5 We recommend:

171. Except in so far as the context otherwise requires any reference to "correction" should include correction by:

(a) the removal of data included in an entry,

(b) the removal of an entry from the statutory pledges record and the transfer of that entry to the archive record,

(c) the replacement of data, or of a copy document, included in an entry,

(d) the restoration of data, or of a copy document, to an entry, or

(e) the restoration of an entry (whether or not by removing it from the archive record and transferring it to the statutory pledges record).

(Draft Bill, s 105(1))

Correction by Keeper

33.6 We consider that the recommendation which we made earlier[4] enabling the Keeper to correct the assignations record where there is a manifest inaccuracy should be mirrored in relation to the statutory pledges record. This would enable the Keeper, for example, to deal with frivolous or vexatious registrations or where the record has been affected by computer malfunction. In principle, as for the assignations record, the Keeper might make a correction using this power because the secured creditor has made an application for this to be done. In practice, however, we would expect secured creditors to apply for corrections under the automated system which we recommend below.[5]

33.7 We recommend:

172. (a) Where the Keeper becomes aware of a manifest inaccuracy in an entry in the statutory pledges record the Keeper should have to correct the inaccuracy if what is needed to correct it is manifest. If what is needed to correct is not manifest the Keeper should have to note the inaccuracy on the entry.

(b) Where an inaccuracy is corrected by:

(i) removal of the entry the Keeper should have to transfer the entry to the archive record and note on the entry the details of the correction, and its date and time,

(ii) removal or replacement of data included in the entry or by replacement of a copy document the Keeper should have

[4] See paras 9.12–9.22 above.
[5] See paras 33.11–33.22 below.

to note on the entry the details of the correction, and its date and time,

(iii) replacement of a copy document, the Keeper should have to transfer it to the archive record.

(c) Where the Keeper effects a correction, the Keeper should have to notify each person specified for these purposes by RSP Rules and any other person whom the Keeper considers it appropriate to notify that the correction has been effected.

(Draft Bill, s 102)

Correction of the statutory pledges record by order of a court

33.8 Once again we envisage a scheme based on the provisions for the RoA which we set out above.[6] This would apply where, for example, a statutory pledge has been reduced by a court order, for example, where there has been fraud. The court would order the Keeper to expunge it from the statutory pledges record.

33.9 We recommend:

173. (a) Where a court determines that the statutory pledges record is inaccurate it should have the power to direct the Keeper to correct it.

(b) In connection with any such correction, the court should be able to give the Keeper such further direction (if any) as it considers requisite.

(c) The Keeper should be required to note on the relevant entry that it has been corrected and the details of the correction, including the date and time. Where the correction requires the removal of the entry or of a copy document the Keeper should have to transfer it to the archive record.

(d) Where the Keeper effects a correction, the Keeper should have to notify each person specified for these purposes by RSP Rules and any other person whom the Keeper considers it appropriate to notify that the correction has been effected.

(Draft Bill, s 103)

Keeper's right to appear and be heard in proceedings in relation to inaccuracies

33.10 There should be the same rules here as for the RoA.[7] We recommend:

[6] See paras 9.23–9.27 above.
[7] See paras 9.28–9.29 above.

174. The Keeper should be entitled to appear and be heard in any civil proceedings, whether before a court or tribunal, in which is put in question (either or both):

(a) the accuracy of the statutory pledges record,

(b) what is needed to correct an inaccuracy in that record.

(Draft Bill, s 104)

Correction by secured creditor

33.11 For corrections in the assignations record we recommended that involvement by the Keeper's staff should be required.[8] Our reasoning for this was that an assignation is a transfer of property and that transfers cannot be extinguished. Once an assignation is registered it should stay on the register. But correction should be possible for errors such as uploading the wrong assignation document, or submitting wrong data to the Keeper. The Keeper would require to play an active role in considering applications for corrections.

33.12 This is markedly different from the position under UCC–9 and the PPSAs etc where the register is essentially fully automated.[9] Secured creditors register an initial notice electronically. This is often known as a "financing statement". Secured creditors then make any correction or register any juridical act (for example restriction to particular types of asset) in relation to a security interest to which the notice relates by means of a further notice. This is often known as a "financing change statement".[10] This approach can be seen to conflate registration of corrections and juridical acts.

33.13 In contrast our scheme deals with these separately. The registration of juridical acts is dealt with in Chapter 23 above. In contrast, the correction procedure is to be used for inaccuracies, where the register does not reflect the true position in fact or law. Examples of this would be where the data which has been registered in respect of the statutory pledge is erroneous, such as where the provider's details are wrong or where the register, in stating that a statutory pledge subsists, is wrong because the statutory pledge has been discharged off-register.

33.14 A statutory pledge, being a security right, has a finite existence. This means that there must be a way of removing it from the register. That way is correction.

33.15 An argument against allowing correction by the secured creditor by means of an automated procedure is that the register might be corrected by mistake or even deliberately when there is no inaccuracy. This is our concern in relation to assignations: the entry for an effectively registered assignation could simply be removed and the registered evidence of the transfer would be gone.[11] In the case of statutory pledges, however, it would be the registered evidence of the subsistence of a right in security which would no longer be there.

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[8] See Chapter 9 above.
[9] Not quite fully. For example, removal of frivolous or vexatious registrations or dealing with administrative error, such as where the computer system fails, require human intervention.
[10] See eg NZ PPSA 1999 s 135.
[11] Albeit it would be kept by the archive record. But that record would not be directly searchable. See para 34.2 below.

Good faith third parties would be protected by the recommendations which we recommend in Chapter 32.[12] Therefore an incorrect correction would not prejudice such parties.

33.16 We have come to the conclusion that an automated correction procedure should be possible. The advantages of this are the same as for automated registration of the statutory pledge or amendments in relation to it, as well as of assignations.[13] We propose a similar procedure as for registration.

33.17 The application would be made by or on behalf of the secured creditor. Where the statutory pledge has been assigned the former creditor should be able to make the correction as it would be accredited by the Keeper's computer system in relation to the entry.[14]

33.18 The Keeper would be required to accept the application if it complied with the relevant RSP Rules and the appropriate fee were paid. The application otherwise would have to be rejected.

33.19 If the application was accepted the Keeper would have to correct the entry accordingly and issue the applicant with a written statement verifying the correction. RSP Rules would set out the form of the verification statement, which would include the date and time of the correction. Importantly, we think that the statement should also be sent by the Keeper's computer system to the provider so that it is notified that a correction has been made. Imagine, for example, that the secured creditor carelessly or maliciously uses the automated correction procedure to widen incorrectly the asset classes over which the statutory pledge has been granted.[15] If the provider is notified it would be possible for a challenge to this to be made. Effective notification here to providers relies on their electronic contact details being correct. Thus earlier we recommended a right for the provider to see a copy of the verification statement in relation to the original registration of the statutory pledge so that these details can be checked.[16]

33.20 Where the correction sought is for removal of the entry, for example where the statutory pledge had been previously extinguished off-register, the Keeper would transfer it to the archive record and note the date and time of the removal. For other corrections, the details including the date and time would be added to the entry, which would remain in the statutory pledges record.

33.21 The automated procedure would only be available for an entry that was in the statutory pledges record. If an entry were moved to the archive record by mistake then application could in principle be made to the Keeper (or court) under the procedures described earlier,[17] but it is far more likely in practice that the statutory pledge would simply be re-registered.

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[12] These recommendations are not mirrored in the RoA. See para 8.14 above.
[13] See paras 6.31–6.44 and 29.24 above.
[14] See para 30.17 above.
[15] This possibility could perhaps also be dealt with by RSP Rules preventing correction to increase the asset classes under the automated procedure, so that such a correction would require an application under the "manifest inaccuracy" route recommended in paras 33.6–33.7 above and thus the involvement of the Keeper's staff.
[16] See para 30.23 above.
[17] See paras 33.6–33.9 above.

33.22 We recommend:

175. (a) The secured creditor should be able to apply for correction of the entry for the statutory pledge in the statutory pledges record.

(b) The Keeper should be required to accept an application if it conforms to RSP Rules in relation to applications and the prescribed fee is paid or the Keeper is satisfied that it will be.

(c) Where these requirements are not satisfied, the Keeper should be required to reject the application and inform the applicant accordingly.

(d) On accepting an application for correction of the statutory pledges record the Keeper should be required to correct the entry accordingly, and issue to the applicant and to the provider of the statutory pledge a written statement verifying the correction.

(e) The verification statement should conform to such RSP Rules as may relate to the statement and include both the date and time of the correction and the registration number allocated to the entry to which the application relates.

(f) The Keeper should be required to note on the relevant entry that it has been corrected and the details of the correction, including the date and time. Where the correction requires the removal of the entry the Keeper should have to transfer it to the archive record.

(Draft Bill, s 100)

Demands for corrections

33.23 The register could contain an inaccuracy which prejudices (a) the provider or (b) a third party. An example of (a) would be where the secured obligation has been performed[18] but the statutory pledge has not been removed from the register. Another example would be where property has been released from the statutory pledge but the entry for it still refers to that property.

33.24 An example of (b) would be where a statutory pledge granted by Philip is mistakenly registered against Paul. Thus someone searching the RSP against Paul would find the entry and this could affect his ability to obtain credit.[19] Another example would be where encumbered property is identified by reference to a unique number (most likely a VIN in respect of motor vehicles).[20] An entry which refers to the wrong number and in consequence

[18] This would typically be where the secured obligation is a fixed sum which has been paid. Under the accessoriness principle the security is extinguished because it does not secure anything. In commercial practice security rights are normally granted for all sums due and to become due. Such security rights remain valid until discharged because although there may be no present indebtedness they are capable of securing a debt which may subsequently arise.

[19] Even with the constitutive document granted by Philip on the register third parties would need to be persuaded that the entry is a mistake and that it is the data and not the document which is wrong.

[20] See para 30.7 above.

to property belonging to another person would prejudice the ability of that person to use that asset as collateral or indeed even to sell it.

33.25 There are various possible ways of dealing with this situation. First, the provider or third party could attempt to contact the secured creditor informally and ask for the correction to be made. But there might be no response. Secondly, the Keeper could be approached. In the case of manifestly inaccurate entries such as where there has been a vexatious registration the Keeper would probably make the correction.[21] But in other cases the Keeper would be unwilling to intervene as the Keeper does not act quasi-judicially. Thus the determination of factual questions such as whether the secured obligation has been performed or whether property has been released is not for the Keeper. Thirdly, a court order could be sought requiring the Keeper to correct the register.[22] But this could be an expensive option.

33.26 The way in which several of the PPSAs deal with this issue is by means of a procedure whereby a formal demand can be made to the secured creditor to register a financing change statement to correct the inaccuracy.[23] The details of the procedure vary in the different jurisdictions but essentially where such a demand is made the secured creditor is required to comply with it within a specified period and correct the registration, or justify why the registration should be maintained. In several jurisdictions notably in Canada (but not Ontario) and New Zealand the secured creditor requires to obtain a court order confirming that the registration should not be corrected. The Statutory Review of the Australian PPSA recommended that it should be amended to adopt the same approach.[24] At first sight this may seem onerous on the secured creditor not least because a provider might be making a demand spuriously. But we understand that the system works well in practice. Providers are highly unlikely to make a groundless demand because in doing so they would damage their relationship with their bank or other lender. Moreover, they would have to bear the bank's costs. The procedure enables a party who is prejudiced by an inaccurate registration a relatively quick and inexpensive way of having the register corrected. We consider that it would be beneficial to have an equivalent procedure in the RSP.

33.27 The procedure should be available, first, to a person incorrectly identified in an entry in the statutory pledges record as a provider or co-provider and second, to a person with a right in property which is incorrectly identified in an entry as being encumbered property. The person should be able to issue a notice to the person identified in the entry as the secured creditor. The notice would demand that the entry is corrected within a specified period of time. We think that this time should not be any less than 21 days.[25] The demand should be issued on a prescribed form which would have notes as to its completion.

33.28 An issue which requires consideration is that the person identified as the secured creditor may no longer be the secured creditor because the statutory pledge has been

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[21] See paras 33.6–33.7 above.
[22] See paras 33.8–33.9 above.
[23] See eg NZ PPSA 1999 ss 162–169, on which see Gedye, Cuming and Wood, *Personal Property Securities in New Zealand* 507–518 and the Australian PPSA 2009 ss 177–182, on which see Allan, *The Law of Secured Credit* 494–496. For the Canadian PPSAs see Cuming, Walsh and Wood, *Personal Property Security Law* 337–340. And see also the Belgian Pledge Act of 11 July 2013 art 39 (which provides for art 33 of the new Book III title XVII of the Civil Code).
[24] Australian Statutory Review 2015 para 6.10.5.8.
[25] This is similar to the period in New Zealand, which is 15 working days. See NZ PPSA 1999 s 163. In Australia the period is only five working days. See Australian PPSA 2009 s 179(1)(b).

assigned. Earlier we recommended that an assignation could take place without registration as is the case for floating charges and for security interests under UCC–9 and the PPSAs.[26] We understand that in the jurisdictions which have change demand procedures an assignor secured creditor would ensure that it alerted the assignee secured creditor of the demand, because otherwise they would have a claim for loss suffered if the security interest becomes unperfected as a result of the relevant notice being removed from the register.[27] Further, although an assignation of a statutory pledge is not registrable it would also be possible to update the entry by means of a correction, meaning that it would be the assignee who would receive the notice.

33.29 A secured creditor should not be entitled to charge a fee for making the correction.[28] The person making the demand would normally be doing so because the inaccuracy in respect of which correction is sought is causing prejudice and therefore it does not seem reasonable that the cost is met by that person.

33.30 Where following the expiry of the specified period the demand has not been complied with the person making it should be entitled to apply to the Keeper for correction. The application would require to conform to RSP Rules made in respect of such applications.

33.31 On receipt of the application the Keeper should be required to do several things. First, the Keeper should have to serve a notice on the person identified in the entry as the secured creditor. This would state that the Keeper intends to correct the record on a date specified in the notice (which could not be fewer than 21 days after the date of the notice). Secondly, the Keeper should have to note the details of the application and the date on which it was received in the relevant entry. Thirdly, the Keeper should be required to issue the applicant with a verification statement confirming receipt of the application. Fourthly, the Keeper should have to notify the person identified in the entry as the provider of the receipt of the application if that person is not the applicant. This might happen where the applicant is a third party owner of property identified in the entry.

33.32 We noted earlier that under the change demand procedures in several jurisdictions the register will be corrected unless the secured creditor obtains a court order within a 21-day period requiring the registration to be maintained. We canvassed this approach with our advisory group and in our draft Bill consultation in July 2017, but it drew significant criticism for being too short a period. In response to this, we recommend now that the secured creditor should, prior to the minimum 21-day period specified in the Keeper's notice elapsing, only be required to apply to the court to oppose the correction. If such an application is made the Keeper should have to be notified within that period and the court should not be able to consider the matter unless satisfied that the Keeper has been duly notified. Were this to be otherwise there is a risk that the Keeper would make the correction because she was unaware that an application had been made. The court would ultimately have to determine whether the record should be corrected or not.

33.33 Where the correction is to remove the entry it would have to be transferred to the archive record. In other cases where only data or a document is to be removed then the entry would remain in the statutory pledges record. The Keeper should be required to notify,

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[26] See paras 23.41–23.48 above.
[27] We are grateful to Professor Catherine Walsh for her assistance.
[28] See the NZ PPSA 1999 s 169 (although this provision is subject to the agreement of the parties).

in so far as it is reasonable and practicable to do so, any persons specified by the RSP Rules for these purposes, that the correction has been made. The Rules would be likely to specify the person identified as the secured creditor and the applicant, and perhaps others. The Keeper should also have a discretion to notify any other person whom the Keeper considers it appropriate to notify.

33.34 We recommend:

176. (a) A person who:

(i) is identified incorrectly as the provider, or as a co-provider, of a statutory pledge in an entry in the statutory pledges record, or

(ii) holds a right in property identified incorrectly as the encumbered property in an entry in the statutory pledges record

may issue a demand in a prescribed form to the person identified in the entry as the secured creditor that the person so identified apply to the Keeper for correction of the statutory pledges record.

(b) Such a demand should require to specify a period (being not less than 21 days after it is received) within which it must be complied with.

(c) No fee may be charged by the person identified as the secured creditor for such compliance.

(d) Where the demand is not complied with the person making it should be able to apply to the Keeper for the correction.

(e) The application should require to conform to such RSP Rules as may relate to it.

(f) On receiving an application the Keeper should be required to:

(i) serve a notice on the person identified in the entry as the secured creditor stating that the Keeper will correct the record on a date specified in the notice (being a date no fewer than 21 days after the date of the notice),

(ii) note on the relevant entry that an application has been received and include in that note the details of the correction sought and the date of receipt,

(iii) issue to the applicant a written statement verifying that the application has been received, and

(iv) notify the person identified in the entry as the provider (if a different person from the applicant) that the notice mentioned in (i) has been served.

(g) The person identified as the secured creditor should have the right to apply to the court prior to the date specified in the notice to oppose the making of the correction and on making any such application should have to notify the Keeper.

(h) The court should be able to direct whether the entry should be corrected or left unchanged, but only if satisfied that the Keeper has been notified of the application to the court prior to the date specified in the notice.

(i) If the Keeper does not receive such notification prior to the date specified in the notice, the Keeper should be required to make the correction on that date.

(j) The Keeper should be required to note in the relevant entry that it has been corrected and the details of the correction, including the date and time. Where the correction requires the removal of the entry the Keeper should have to transfer it to the archive record.

(k) Where the Keeper effects a correction, the Keeper should have to notify each person specified for these purposes by RSP Rules and any other person whom the Keeper considers it appropriate to notify that the correction has been effected.

(Draft Bill, s 101)

Effect of correction

33.35 Many of the corrections mentioned above would be to remove bad data and entries. Here the correction would simply make the register reflect legal reality.

33.36 But where the original registration of a statutory pledge has been ineffective a correction by the secured creditor would put matters right and render the registration effective. For example, a wrong copy of the constitutive document could be replaced with the correct one. The result would be that the pledge would then be created at this time (other than as regards after-acquired assets or assets not yet identifiable as being encumbered property).

33.37 We recommend:

177. A registration which is ineffective should become effective if and when the entry is corrected.

(Draft Bill, ss 95(3) and 96(3))

Date and time of correction

33.38 Finally, the register should always state the date and time of correction. This is particularly important in circumstances where the correction has substantive effect, in other words makes an ineffective registration effective. We recommend:

178. A correction should be taken to be made on the date and at the time which are entered for it in the register.

(Draft Bill, s 105(2))

Chapter 34 Register of Statutory Pledges: searches and extracts

Introduction

34.1 In Chapter 10 above we dealt with the issues of searches and extracts in the Register of Assignations. Almost identical considerations apply in relation to the Register of Statutory Pledges and unsurprisingly we take the same approach to these. We envisage once again that searches would be carried out electronically under an automated system and would not require the involvement of the Keeper's staff.

Searches: general

34.2 An entry in the statutory pledges record would contain (a) data; (b) the constitutive document of the statutory pledge; and (c) any amendment document that has been registered. We expect that amendment documents would be relatively unusual.[1] As with the RoA, it would be the data which would be directly searchable using the Keeper's computer system. In contrast the archive record would not be directly searchable, but it would be possible to obtain an extract of an entry in that record by means of an application to the Keeper.[2]

34.3 The RSP would be primarily (although, in contrast to the RoA, not exclusively) a person-based register. Searches would normally be carried out against the provider of the statutory pledge. As is the position under UCC–9 and the PPSAs we do not recommend that searching should be available against secured creditors on the basis that this would enable information on a financial institution's customers to be garnered too simply by a competitor.[3]

34.4 For searches against providers we recommend the same approach as for assignors in the RoA.[4] There would be three possibilities. First, a search could be made against the provider's name. Secondly, a search could be made against the provider's name *and* date of birth. Thirdly, a search could be made by reference to the unique number of the provider where the provider is a person required by RSP Rules to be identified in the statutory pledges record by such a number. We would expect the Rules to prescribe UK companies and LLPs, but there may be further possibilities.

34.5 Sometimes encumbered property would have a unique serial number, such as a VIN in the case of motor vehicles, or a registration number in the case of a patent. RSP Rules should be able to specify relevant asset types which have such numbers. Where such specification is made the secured creditor in applying for registration can then input the

[1] Amendment documents that are registrable may either (a) increase the extent of the secured obligation; or (b) add property to the encumbered property.
[2] See paras 34.14–35.15 below.
[3] But in the interests of flexibility the provision which we recommend below allowing the register to be searched by other factors or characteristics specified in RSP Rules could in theory be used to allow this.
[4] See paras 10.4–10.6 above.

number in the relevant data field in the application. The advantage of doing this is that the RSP can then be directly searchable against that number and it does not matter who the current holder is. This to some extent can obviate the issue of supervening inaccuracies in the register when the provider changes name or makes an unauthorised transfer of the property to a third party.[5]

34.6 Finally, it should also be competent to search the statutory pledges record by reference to the unique number for an entry and by reference to any other factor or characteristic specified by RSP Rules.

34.7 We recommend:

> **179. The statutory pledges record should be searchable only:**
>
> **(a) by reference to any of the following data in the entries contained in that record:**
>
> **(i) the names of providers,**
>
> **(ii) the names and dates of birth of providers who are individuals,**
>
> **(iii) the unique numbers of providers required by RSP Rules to be identified in the statutory pledges record by such a number,**
>
> **(b) if RSP Rules require or permit the encumbered property to be identified by a unique number by reference to that number,**
>
> **(c) by reference to registration numbers allocated to entries in that record, or**
>
> **(d) by reference to some other factor, or characteristic, specified for these purposes by RSP Rules.**
>
> (Draft Bill, s 106(2))

Who can search?

34.8 As for the RoA,[6] our view is that the RSP should be searchable by anyone on complying with RSP Rules and making payment to the Keeper.

34.9 We recommend:

> **180. A person should be able to search the statutory pledges record if the search accords with RSP Rules and either such fee as is payable for the search is paid or the Keeper is satisfied that it will be paid.**
>
> (Draft Bill, s 106(1))

[5] See Chapter 32 above.
[6] See paras 10.11–10.17 above.

Search facilities

34.10 Once again we propose the same approach as for the RoA.[7] There would require to be an "official" search facility for the purposes of the "seriously misleading" test in relation to effective registration. There should be discussion with stakeholders when the register is being set up as to whether an "exact match" or a "close match" approach is taken, and the matter dealt with in RSP Rules. It should also be possible for the Keeper to offer other forms of search.

34.11 We recommend:

181. (a) The Keeper should be required to provide a search facility in relation to which the search criteria are specified by RSP Rules, but may provide such other search facilities, with such other search criteria, as the Keeper thinks fit.

(b) "Search criteria" should be defined as the criteria in accordance with which what is searched for must match data in an entry in order to retrieve the entry.

(Draft Bill, s 107)

Printed search results

34.12 In line with the position in comparator legislation[8] it should be possible to use a printed search result as evidence of data on the register. In the absence of challenge, this should be sufficient proof of a registration or correction.

34.13 We recommend:

182. A printed search result which purports to show an entry in the statutory pledges record:

(a) should be admissible in evidence, and

(b) in the absence of evidence to the contrary, should be sufficient proof of:

(i) the registration of the statutory pledge, or amendment to the entry in the statutory pledges record, to which the result relates,

(ii) a correction of the entry in the statutory pledges record to which the result relates, and

(iii) the date and time of such registration or correction.

(Draft Bill, s 108)

[7] See paras 10.22–10.29 above.
[8] See para 10.30 above.

Extracts

34.14 There should be a facility to apply to the Keeper for extracts, as with the RoA.[9] This would include the archive record, where the entry for a statutory pledge would be transferred following a correction to take account of its discharge. The archive record would also be the destination of an entry which has been removed from the statutory pledges by means of a correction.

34.15 We recommend:

183. (a) Any person should be able to apply to the Keeper for an extract of an entry in the register.

(b) The Keeper should be required to issue the extract if such fee as is payable for issuing it is paid or arrangements satisfactory to the Keeper are made for payment of that fee.

(c) The Keeper should be able to validate the extract as the Keeper considers appropriate.

(d) The Keeper should be able to issue the extract as an electronic document if the applicant does not require that it be issued as a traditional document.

(e) The extract should be accepted for all purposes as sufficient evidence of the contents, as at the date on which and time at which the extract is issued (being a date and time specified in the extract).

(Draft Bill, s 109)

[9] See paras 10.32–10.34 above.

Chapter 35 Register of Statutory Pledges: miscellaneous

Introduction

35.1 In this chapter we consider miscellaneous matters in relation to the register, namely (1) information duties; (2) duration of registration and decluttering; (3) archiving; (4) liability of the Keeper and other parties for errors and breach of duties; and (5) RSP Rules.

Information duties

General

35.2 Similar issues arise here as for the Register of Assignations.[1] The information which appears in entries in the Register of Statutory Pledges may not be up-to-date. The secured creditor may have discharged the pledge by means of a written statement but not corrected the register.[2] Earlier in this Report we recommended that the assignation of a statutory pledge should not require registration to take effect.[3] It should therefore be possible to seek information as to whom the statutory pledge has been assigned. As under the PPSAs and other comparator legislation we consider that there should be limited information duties to limited classes of third party.

What information?

35.3 We think that the information which may be requested should fall into three categories. The first would be whether a particular item of property is still encumbered by the statutory pledge. As with the RoA[4] we do not think that it should be possible to "fish" for a list of all the encumbered property. The party making the request should have to specify particular property. The second would be a description of the secured obligation, as this may well not be fully apparent from the entry if it is described in the constitutive document by reference to off-register documentation.

35.4 The third would be information as to the holder of the statutory pledge. Thus where the person identified in the entry as the secured creditor receives a request as to whether certain property is encumbered and that person has assigned the statutory pledge it should be required to supply the details of the assignee and indeed, if known, any subsequent assignees.[5]

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[1] See paras 11.2–11.17 above.
[2] See paras 23.49–23.54 above.
[3] See paras 23.41–23.48 above.
[4] See para 11.5 above.
[5] As under DCFR IX.–3:320(3).

Who can request?

35.5 There would be a limited list of persons entitled to information and that list would be similar to the equivalent list for the RoA.[6] It would include (a) those who have the consent of the provider, for example, a prospective secured creditor; (b) those who are entitled to execute diligence against the property, even if a charge for payment has not been executed; and (c) those who are prescribed by the Scottish Ministers, such as perhaps insolvency officials[7] and executors.

35.6 In addition we think that any person with a right in the encumbered property should be entitled to request information, for example another secured creditor. This category is not required in the equivalent provisions for assignation because it is not possible to have a subordinate property right in an incorporeal such as a claim.[8]

How should a request be made?

35.7 The request would be made to the person identified in the entry as the secured creditor, normally we expect by electronic communication.

35.8 We recommend:

184. (a) An entitled person should be entitled to request from the person identified in an entry in the statutory pledges record as the secured creditor:

(i) if that person is the secured creditor, a written statement:

(a) as to whether or not property specified by the entitled person is, or is part of, the encumbered property; or

(b) describing the secured obligation, or

(ii) if that person has assigned the statutory pledge, the name and address of the assignee and (as the case may be and in so far as known) the names and addresses of subsequent assignees.

(b) The following should be entitled persons:

(i) a person who has a right in the property so specified,

(ii) a person who has the right to execute diligence against that property (or who is authorised by decree to execute a charge for payment and will have the right to execute

[6] See paras 11.6–11.8 above.
[7] Although we are aware that insolvency officials already have powers to examine the debtor and other relevant parties.
[8] See para 17.5 above.

diligence against that property if and when the days of charge expire without payment),

(iii) a person who is prescribed for these purposes, and

(iv) a person who has the consent of the person identified in the entry as the provider.

(Draft Bill, s 110(1) to (2))

Duty to comply

35.9 The rules here would be similar to those for the RoA. The person identified in the entry as the secured creditor would have 21 days to comply. They could seek an extension to that period from the court. It would be entitled to grant the extension if it was satisfied in all the circumstances that it would be unreasonable for there to be compliance within that period. The court could also be asked to rule that the request need not be complied with, but again would have to be satisfied that in all the circumstances requiring compliance would be unreasonable. For example, while the person seeking the information is entitled to do so because they have the provider's consent they may have no objective need to have the information.

35.10 There should be no duty to comply if it is manifest from the entry that the property in question is not encumbered.[9] For example, in an entry it is stated that the encumbered property is a yacht. It is therefore directly apparent that no car is encumbered. Similarly, if the full terms of the secured obligation can be determined from the entry the secured creditor should not have to respond to a request for a description of that obligation.

35.11 Further, there should be no duty to comply if it is manifest that the registration is ineffective. For example, if the entry states that the secured creditor (in whose favour the statutory pledge was granted and not an assignee[10]) is Martin but the constitutive document is granted in favour of Neil then no property is encumbered because of the seriously misleading inaccuracy.

35.12 We recommend also that if the same person has made the same request within the last three months and there has been no change, no reply should be required.[11]

35.13 If none of the exceptions are relevant and the person identified in the entry as the secured creditor fails to supply the requested information the entitled person should be entitled to seek a court order requiring them to do so within 14 days. The court should grant the order if it is satisfied that there is no reasonable excuse for failing to supply it. The recommendations so far here mirror those which we made earlier in relation to the RoA.[12] But for the statutory pledge we considered whether the court should also have the power to penalise the non-complying party by extinguishing the statutory pledge and directing the

[9] DCFR IX.–3:320(5)(a).
[10] If the statutory pledge has been assigned and the details of the secured creditor corrected to reflect this the secured creditor named in the entry would be different from the one in the constitutive document.
[11] DCFR IX.–3:320(5)(a).
[12] See para 11.11 above.

Keeper to remove it from the register. The power to order deletion from the register for failure to comply is found in comparator legislation.[13] We did not recommend it in relation to the RoA because the concept of the extinction of a transfer is incoherent. In theory the order could effect a re-transfer but this would be complicated because the claim may have been further assigned. In response to our draft Bill consultation in July 2017 R3 criticised the idea that a statutory pledge should be extinguished for failure to comply with information duties and similar views were expressed by some of our advisory group. We have therefore decided against such a power.

35.14 We recommend:

185. (a) An information request should require to be complied with within 21 days of its receipt, unless:

(i) the court is satisfied that in all the circumstances this would be unreasonable and either extends the 21-day period or exempts the recipient from complying with the request in whole or in part,

(ii) it is manifest from the entry that the property specified in the notice has not been encumbered by the statutory pledge or that the registration is ineffective,

(iii) where a request has been made for a description of the secured obligation where it is manifest from the entry alone what the extent of that obligation is, or

(iv) the same request has been made by the same person within the last 3 months and the information supplied in response to the last request has not changed.

(b) The recipient should be entitled to recover from the requester any costs reasonably incurred in complying with the request.

(c) If the court is satisfied on the application of the requester that the recipient has not complied with the duty to provide information without reasonable excuse it should by order require that the recipient complies within 14 days.

(Draft Bill, s 110(3) to (7))

[13] See eg NZ PPSA 1999 s 182. Although the effect is less extreme because the security interest becomes unperfected rather than extinguished. But our recommended scheme does not recognise the attachment/perfection distinction as it was rejected by consultees. See para 18.45 above. An alternative approach taken by the DCFR IX.–3:323 is that if information is not provided the acquirer takes the right free of the security.

Where incorrect information is supplied

35.15 Imagine that Bank A holds a statutory pledge over the car fleet of the Rothienorman Taxi Company Ltd. Bank B is willing to lend the Company money but also wants to take security over the cars. The Company informs Bank B that Bank A has restricted the statutory pledge off-register so that it no longer encumbers any Volkswagens. This is in fact not true. But with the Company's permission Bank B makes an information request to Bank A in relation to the Volkswagens. Bank A mistakenly advises that these vehicles are no longer encumbered. Bank B promptly takes a statutory pledge over them. What should be the position?

35.16 Below we recommend that there should be statutory liability for loss caused to a party by reason of incorrect information being supplied in response to a request, which would apply where the secured creditor failed to take reasonable care.[14] But to make such a claim would more than likely require court action. Drawing on the DCFR we consider that the effect of supplying incorrect information that an item of property is unencumbered when in fact it is encumbered should result in the pledge being extinguished in certain circumstances.[15] These would be where the entitled person who received the wrong information went on to acquire the property or a right in it within three months of receipt of the information provided that they were in good faith. Hence if the entitled person knew by whatever means that the information was wrong it would not be protected.

35.17 In formulating this rule we have drawn on our earlier recommendations in relation to supervening inaccuracies.[16] We accept, however, that policy choices here are difficult and that there are arguments that the protection should be narrower and apply only where the property is acquired rather than also where a security right is acquired in it. Similarly, in the case of the acquisition of a subsequent security it can be argued that the statutory pledge should only be ineffective as regards the creditor who was given the wrong information rather than extinguished. The broader approach, however, encourages more firmly the supply of accurate information.

35.18 We recommend:

186. Where:

(a) an entitled person in response to an information request is incorrectly informed that the property specified in the request is unencumbered by the statutory pledge, and

(b) within 3 months of being so informed acquires in good faith

(i) the property so specified or any part of it,

(ii) a right in that property (or any part of it),

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[14] See paras 35.35–35.36 below.
[15] DCFR IX.–3:322(1).
[16] See Chapter 32 above.

on the acquisition the statutory pledge is extinguished as regards the property or part.

(Draft Bill, s 110(8) to (9))

Where a statutory pledge has been assigned

35.19 If in response to an information request the person identified in the statutory pledges record as the secured creditor advises that the statutory pledge has been assigned and provides the details of the assignee, the information duties set out above should also apply to that person. For example, that person too should be required to advise whether particular property is encumbered. We recommend:

187. The duties to provide information should also apply to any assignee of the statutory pledge.

(Draft Bill, s 110(10))

Duration of registration and decluttering

35.20 It is generally the case in the Land Register that a standard security will be discharged when the loan is repaid, and thus be removed from the register. And purchasers of land will normally be unwilling to proceed until they (or perhaps more accurately, their solicitors) are satisfied that any standard security granted by the seller will be discharged.

35.21 The experience as regards moveable property is different, no doubt partly because there is not registration of title to moveables[17] and thus no comparator to registration of title to land. For example, in England and Wales, the discharge of a bill of sale is commonly not registered.[18] This leads to a cluttered register. The risk of cluttering is particularly high where a functional approach is taken to security rights, so that registration is required for any transaction functioning as a security. This is dealt with in various ways.

35.22 One is for registration to be time-limited, with the possibility of renewal. If there is no renewal the entry lapses. This is the position under, for example, UCC–9 (5 years);[19] the NZ PPSA (5 years);[20] DCFR Book IX (5 years);[21] and the Belgian Pledge Act (10 years).[22] Another is for the registration to be for such period as is chosen by the applicant, with higher fees for longer periods. This is the position under the Australian PPSA, where registrations in respect of consumer and serial-numbered property can have a maximum duration of

[17] With some minor exceptions, notably ships. See Chapter 21 above.
[18] In 2007 and 2008 fewer than 20 memorandums of satisfaction were registered, despite almost 80,000 bills of sale being registered. See Department for Business, Innovation and Skills, A Better Deal for Consumers: Consultation on proposal to ban the use of bills of sale for consumer lending (2009) p 34 available at https://www.gov.uk/government/consultations/consultation-on-proposal-to-ban-the-use-of-bills-of-sale-for-consumer-lending. See also Law Com Report No 369 paras 6.70–6.86 for recommendations in relation to the proposed new goods mortgages, including a ten-year lapsing period where the encumbered property is not a vehicle.
[19] UCC § 9–515.
[20] NZ PPSA 1999 s 153. A shorter period can be chosen.
[21] DCFR Book IX.–3:325.
[22] Belgian Pledge Act of 11 July 2013 art 33 (which provides for art 41 of the new Book III title XVII of the Civil Code).

seven years, but for other types of property there is no maximum.[23] The Canadian PPSAs generally allow applicants for registration to choose the duration, from one year to infinity.[24] The UNCITRAL Model Law on Secured Transactions has three possible approaches: (A) fixed period; (B) period chosen by applicant; and (C) period chosen by applicant up to a maximum.[25]

35.23 In a non-functional system, the approach is different. Registration under Part 25 of the Companies Act 2006 is indefinite.[26] This is also the position under the draft Secured Transactions Code prepared by the Financial Law Committee of the City of London Law Society.[27] In its Report on Bills of Sale, the Law Commission for England and Wales does not recommend any fixed period of registration for the new "goods mortgage" in respect of motor vehicles. Rather, it is of the view that debtors are sufficiently protected if a creditor fails to remove the mortgage from the relevant asset finance registry by being able to complain to the Financial Conduct Authority. But it recommends a 10 year lapse period for registrations at the High Court of goods mortgages over assets other than motor vehicles.[28]

35.24 In the Discussion Paper we said that while the issue was an open one, we inclined to the UCC–9 approach, on the basis that the inconvenience to lenders of having to renew a registration every five years is outweighed by the inconvenience of a register choked by dead entries.[29] We asked consultees for their views.

35.25 Most of our consultees opposed the suggestion that a registration should lapse after a certain period unless renewed. These included the Faculty of Advocates and the Law Society of Scotland. The WS Society argued that it would be "a recipe for confusion. There is no more justification for entries lapsing than for floating charges or standard securities lapsing." There was limited support for a system under which the applicant had to specify a registration period. Most of our advisory group preferred a system under which registration entries last indefinitely. Their arguments are similar to those made during the statutory review of the Australian PPSA, where stakeholders were generally opposed to a New Zealand-style system of lapse after a certain period. As the reviewer stated: "Respondents argued that the secured parties often have long-term secured relationships with grantors, and that it would be unfair to require those secured parties to re-register part way through the term of that relationship."[30]

35.26 We have concluded that registration in the statutory pledges record in principle should be for an indefinite period, as is the case for standard securities and floating charges. We are in particular persuaded by the fact that the context is different from a functional system of registration, so that the number of registrations would be substantially lower. Nevertheless, we think that the legislation should be future-proofed. There may come a date

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[23] Australian PPSA 2009 s 153.
[24] Although in Ontario for consumer goods the period is limited to five years. See Cuming, Walsh and Wood, *Personal Property Security Law* 353–354.
[25] UNCITRAL Model Law on Secured Transactions Model Registry Provisions art 14.
[26] But see Law Com Report No 296 paras 3.110–3.111.
[27] Although at p 93 in the commentary it is stated that consideration should be given to a mechanism by which a chargor could have a charge removed from the register following release, where the charge cannot be tracked down, perhaps by means of a court application.
[28] Law Com Report No 369, paras 6.70–6.86.
[29] Discussion Paper, para 20.52.
[30] Australian Statutory Review 2015 para 6.92.

many years in the future where the statutory pledges record clearly does need decluttering of "dead" entries. We therefore consider that the Scottish Ministers should have the power by regulations to set a period after which a statutory pledge would be extinguished unless the entry for it is renewed in the meantime. Clearly there should be consultation before that power is used. In particular, we think that there should require to be consultation with the Keeper.

35.27 If the Scottish Ministers did exercise the power there would need to be the ability to renew entries in advance of when the lapse would otherwise take effect. It is possible also that Ministers may wish to have different rules for (a) existing statutory pledges and (b) statutory pledges registered after the power is used. For example, if a ten-year lapse period were introduced as regards existing statutory pledges, the period could be provided to run from the commencement date of the lapse regulation and not the date on which the statutory pledge was registered. Imagine that a statutory pledge is registered in favour of the Ballater Bank on 1 April 2025. On 1 December 2050 a ten-year lapsing rule is introduced. The statutory pledge would lapse on 1 December 2060 unless renewed beforehand.

35.28 Finally, it should be stressed that whereas under the UCC–9/PPSA approach the lapsing of a registration means that the security right is no longer perfected (and in general will not have third party effect), in the RSP the statutory pledge would be entirely extinguished. This is because of the rejection of the attachment/perfection discussed above.[31]

35.29 We recommend:

188. (a) The Scottish Ministers should have power to make regulations specifying a period after which an entry in the statutory pledges record will lapse unless it is renewed.

(b) Before exercising this power, the Scottish Ministers must consult the Keeper.

(Draft Bill, s 99)

Archiving

35.30 In the RoA the purpose of the archive record would be to store entries which have been removed from the assignations record following a correction.[32] Clearly, the RSP would require an archive record to perform this function too. We expect that where a statutory pledge is discharged it should become standard practice for the secured creditor to correct the register to remove it.

35.31 There would be one further case where the archive record would be used. This would be where the Scottish Ministers made regulations for the lapsing of statutory pledges after a certain period of time.[33]

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[31] See paras 18.44–18.49 above.
[32] See paras 11.19–11.21 above.
[33] See paras 35.20–35.29 above.

35.32 We recommend:

189. The archive record should be the totality of all the entries transferred from the statutory pledges record following:

(a) correction to remove an entry, and

(b) lapsing of a statutory pledge under regulations made by the Scottish Ministers,

and should also contain such other information as may be specified by RSP Rules.

(Draft Bill, s 90)

Liability of Keeper and other parties

Introduction

35.33 Earlier we recommended statutory liability rules for the Keeper and other parties in relation to the RoA.[34] We explained that while liability questions could in principle be left to the common law, placing the matter on a statutory footing would provide more certainty. Further, in relation to the Keeper we considered that there should be strict liability.

Liability of Keeper

35.34 The RSP would be managed by the Keeper in a very similar way to the RoA and it would plainly therefore be appropriate for the same liability rules to apply.[35] We set out the basis for these rules above.[36] We recommend:

190. (a) A person should be entitled to be compensated by the Keeper for loss suffered in consequence of:

(i) an inaccuracy attributable to the Keeper in the making up, maintenance or operation of the Register of Statutory Pledges, or in an attempted correction of the register,

(ii) the issue of a statement or notification which is incorrect, or

(iii) the issue of an extract which is not a true extract.

(b) But the Keeper should have no statutory liability:

[34] See paras 11.22–11.42 above.
[35] One difference between the RoA and the RSP is that in the former corrections would always require the intervention of the Keeper's staff. In contrast it would be possible for a secured creditor in the RSP to make a correction using the automated system. But this does not necessitate different liability provisions.
[36] See paras 11.24–11.34 above.

(i) in so far as the person's loss could have been avoided had the person taken measures which it would have been reasonable for the person to take,

(ii) in so far as the person's loss is not reasonably foreseeable, or

(iii) for non-patrimonial loss.

(Draft Bill, s 111)

Liability of certain other persons

35.35 Once again we consider that the same rules should apply as for the RoA.[37] There should be fault-based (rather than strict) liability in certain circumstances. The first would be where a person who has registered a statutory pledge creates an inaccurate entry which causes another person loss, such as a person being identified as a provider when that is not the case. The second would be where the secured creditor fails to respond to a request for information or supplies incorrect information in response to such a request.[38] There would be the same limitations on liability as for the equivalent provisions in relation to the RoA.

35.36 We recommend:

191. (a) Where a person suffers loss in consequence of:

(i) an inaccuracy in an entry in the Register of Statutory Pledges (which is not caused by the Keeper), the person should be entitled to be compensated for that loss by the person who made the application which gave rise to that entry if, in making it, that person failed to take reasonable care, or

(ii) a failure to respond to a request for information under the information duty provisions, or the provision of information in which there is an inaccuracy, the person is entitled to be compensated for that loss by the person who failed to supply the information if that failure was without reasonable cause or if, in supplying it, that person failed to take reasonable care.

(b) But there should be no liability:

(i) in so far as the person's loss could have been avoided had the person taken measures which it would have been reasonable for the person to take,

(ii) in so far as the loss is not reasonably foreseeable, or

[37] See paras 11.35–11.42 above.
[38] On duties to provide information see paras 35.2–35.19 above.

(iii) for non-patrimonial loss.

(Draft Bill, s 112)

RSP Rules

35.37 We explained earlier in relation to the RoA that it is typical in statutes on registration both in Scotland and internationally for there also to be secondary legislation in the interest of flexibility.[39] We therefore recommend that the Scottish Ministers should have the power to make regulations in relation to the RSP, which would be known as "RSP Rules". The power should be a wide-ranging one and should be very similar to that for the RoA.

35.38 We recommend:

192. The Scottish Ministers should, following consultation with the Keeper, be able by regulations to make rules (to be known as "RSP Rules"):

(a) as to the making up and keeping of the register,

(b) as to procedure in relation to applications:

(i) for registration, or

(ii) for corrections,

(c) as to the identification, in any such application of any person or property, including:

(i) how the proper form of a person's name is to be determined, and

(ii) where the person bears a number (whether of numerals or of letters and numerals) unique to the person, whether that number must (or may) be used in identifying the person,

(d) as to the degree of precision with which time is to be recorded in the register,

(e) as to the manner in which an inaccuracy in the statutory pledges record may be brought to the attention of the Keeper,

(f) as to information which, though contained in a constitutive document or amendment document, need not be included in a copy of that document submitted with an application for registration,

[39] See paras 11.43–11.49 above.

(g) as to whether a signature contained in a constitutive document or amendment document need be included in a copy of that document so submitted,

(h) as to searches in the register,

(i) as to information which, though contained in the register, is not to be:

(i) available to persons searching it, or

(ii) included in any extract issued by the Keeper,

(j) prescribing the configuration, formatting and content of:

(i) applications,

(ii) notices,

(iii) documents,

(iv) data,

(v) statements, and

(vi) requests

to be used in relation to the register,

(k) as to when the register is open for:

(i) registration, and

(ii) searches,

(l) requiring there to be entered in the statutory pledges record or the archive record such data as may be specified in the rules, or

(m) regarding other matters in relation to registration, being matters for which the Scottish Ministers consider it necessary or expedient to give full effect to the purposes of the draft Bill.

(Draft Bill, s 114)

Chapter 36 The company charges registration scheme

Introduction

36.1 The company charges registration scheme requires that most security rights granted by companies are registered in the Companies Register.[1] In the Discussion Paper we briefly reviewed the history of the scheme.[2]

36.2 "Charge" is a term in English law for a certain type of security right.[3] English law traditionally did not accept the publicity principle in relation to charges and indeed more widely,[4] but this began to change in the nineteenth century. In particular, there was increasing concern that companies could charge their assets in secret. This led to section 14 of the Companies Act 1900, the modern day successor of which is Part 25 of the Companies Act 2006.

36.3 Originally, the requirement to register company charges did not apply to Scotland. But, when the floating charge was introduced by the Companies (Floating Charges) (Scotland) Act 1961, so too was company charges registration. Thus not only does a floating charge have to be registered, so does a standard security granted by a company. This is even although the standard security requires to be registered in the Land Register. Likewise, where a patent is assigned in security the assignation has to be registered in both the Register of Patents and the Companies Register to be effective against third parties. This requirement for double registration has been trenchantly criticised,[5] but there are many in practice who like the fact that the Companies Register amounts to a "one stop shop" for checking the security rights granted by a particular company.

36.4 In 2004 this Commission recommended that the company charges registration should be abolished and that floating charges should be registered instead in a new Register of Floating Charges. The first part of this recommendation was not accepted by the Department of Trade and Industry.[6] The second part was accepted by the Scottish Government, leading to Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007. But, as we saw above, Part 2 has not been brought into force.[7]

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[1] There are parallel provisions for security rights granted by LLPs and certain other entities, but in the interests of brevity we refer only to companies in the chapter.
[2] Discussion Paper, para 8.1.
[3] See eg Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 1.18.
[4] On this principle, see the Discussion Paper, Chapter 11.
[5] See G L Gretton, "Registration of Company Charges" (2002) 6 EdinLR 146.
[6] A predecessor of the Department for Business, Energy and Industrial Strategy.
[7] See paras 18.23–18.25 above.

Companies Act 2006 Part 25 since 1 April 2013

36.5 As a result in part of the work of the Law Commission for England and Wales,[8] the companies charges registration scheme was overhauled with effect from 1 April 2013.[9] Previously there had been separate versions applying north and south of the border. Now there is a unified scheme. Formerly, the charges which required to be registered were specified. Now all charges must be registered, except where they are expressly excluded. A "charge" includes "a standard security, assignation in security, and any other right in security constituted under the law of Scotland, including any heritable security, but not including a pledge".[10]

36.6 Charges must be registered in the Companies Register within 21 days of their date of creation.[11] That date has different definitions for different types of security right.[12] For standard securities it is 21 days after their date of registration in the Land Register. Prior to 1 April 2016 a standard security would be recorded in the Register of Sasines if the land over which it was being granted was not yet registered in the Land Register. Now only registration in the Land Register is possible, meaning that the land to be encumbered must be registered in that Register in order for the standard security to be created. The purpose of this rule is to speed up completion of the Land Register.[13]

36.7 For other security rights, the deadline is normally 21 days after their date of delivery. For example, if A Ltd grants a floating charge in favour of Bank B, the period runs from when the floating charge document signed by A Ltd is delivered to the bank. Prior to the floating charge being registered, there is thus an "invisibility period". This is something which has been the subject of longstanding criticism.[14] The Bankruptcy and Diligence etc. (Scotland) Act 2007 Part 2 reforms would have eliminated this.[15]

36.8 In a change to the position prior to 1 April 2013, it is necessary to register a certified copy of the charge.[16] The consequences of not registering a charge within the 21-day period are very serious. The charge is void against a liquidator, administrator or a creditor of the company.[17]

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[8] Law Commission for England and Wales, Company Security Interests (Law Com No 296, 2005).
[9] Companies Act 2006 (Amendment of Part 25) Regulations 2013 (SI 2013/600). For discussion, see K G C Reid and G L Gretton, *Conveyancing 2013* (2014) 172–178 and H Patrick, "Charges changing" 2013 JLSS Feb/20.
[10] Companies Act 2006 s 859A(7)(b).
[11] Companies Act 2006 s 859A(4).
[12] Companies Act 2006 s 859E(1).
[13] See Registers of Scotland (Voluntary Registration, Amendment of Fees, etc) Order 2015 (SSI 2015/265) art 3.
[14] See D Bennett, "A Judicial Wet Blanket Upon the Register of Charges" 1967 SLT (News) 153; W W McBryde and D M Allan, "The Registration of Charges" 1982 SLT (News) 177 and Scottish Law Commission, Report on Registration of Rights in Security by Companies (Scot Law Com No 197, 2004) para 1.17.
[15] But see G Yeowart "A register of floating charges over Scottish assets: a new "Slavenburg" problem?" 2012 Journal of International Finance and Banking Law 470 at 471: "experience indicates that the 'invisibility period' is not a serious practical problem . . . Both the Committee of Scottish Clearing Bankers and the British Bankers' Association have also expressed the view that the "invisibility period" is not a significant problem in practice." Nevertheless, the City of London Law Society's draft Secured Transactions Code arts 8 and 32 provide for a charge to be created on registration, which would thus end the invisibility period.
[16] Companies Act 2006 s 859A(3).
[17] Companies Act 2006 s 859H(3).

The statutory pledge and registration in the Companies Register: general

36.9 We recommended above that the statutory pledge should normally require to be registered in the Register of Statutory Pledges.[18] In view of the "included unless expressly excluded" approach of Part 25 of the Companies Act 2006 since 1 April 2013, statutory pledges granted by companies would have to be registered in the Companies Register too.[19] In other words there would require to be double registration. This would also be the position for an assignation in security of a claim by a company completed by registration in the RoA.[20] It would require to be registered in the Companies Register, given the definition of "charge" referred to above.[21]

36.10 In the Discussion Paper we expressed the view that the new security right being proposed should not be registrable under Part 25.[22] Following the 2013 reforms and also the view expressed by our advisory group in relation to the benefits of the "one stop shop" of the Companies Register, we no longer hold to that position.

36.11 We argued, alternatively, in the Discussion Paper that, if the new security right were to be registrable under the company charges registration scheme, the need for double registration should be removed by an order being made by the Secretary of State for Business, Energy and Industrial Strategy under section 893 of the Companies Act 2006. Under the company charges registration scheme there often has to be double registration, for example, for standard securities.[23] Section 893 allows the Secretary of State to make an order whereby registration in the Companies Register will no longer be necessary provided that a system is in place for the transmission from the "special register" (for example, the Land Register) to the Companies Register of the registered information. The effect of such an order would be that those searching the Companies Register would still be able to obtain the same information as at present.

36.12 In 2010 the Department for Business, Innovation and Skills (DBIS), the predecessor of the Department for Business, Energy and Industrial Strategy (DBEIS) set out the criteria which must be satisfied before a section 893 order can be made:

> ''There are several aspects to appropriate information-sharing arrangements. First, Companies House and the specialist registry must share information so that any filing that would have been rejected by Companies House (for example, because it does not include the correct name and number for the company creating the charge or any other required information is missing) is not treated as if registered at Companies House whether or not the specialist registry accepts the registration under its own procedures.
>
> Second, anyone inspecting a particular company's record at Companies House would have to be able to see sufficient information for any charge that has been registered at the specialist register to ensure that third parties are not disadvantaged

[18] See Chapter 23 above. There would be an exception for financial collateral arrangements. See Chapter 37 below.
[19] While the Companies Act 2006 s 859A(7)(b) provides that the registration requirement does not apply to "a pledge" this refers to pledge under the current law ie a possessory pledge.
[20] See Chapter 5 above.
[21] See para 36.5 above.
[22] Discussion Paper, para 20.47.
[23] See para 36.3 above.

by the charge not having been registered at Companies House. This information must be available to all inspecting the company's record, whether online, by bulk download, or by personal enquiry at a Companies House enquiry point; the online record would have to have a link to the relevant entry in the specialist register (see paragraphs 89-93).

Third, the specialist registry must also accept filing of a memorandum of satisfaction (in whole or in part) for any charge registered with it - and this information must be similarly shared with Companies House.

Fourth, these arrangements must not increase costs either for those who register charges or for those who use the information at Companies House to assess the financial status of companies. However the specialist registry's prices would apply to any further inspection of a charge registered with it."[24]

No section 893 order has been made as regards any register. Nevertheless, we took the view in the Discussion Paper that such an order would be desirable.[25]

Consultee responses

36.13 We asked consultees whether they agreed that if a new moveable security is introduced, which is created by registration, a section 893 order should be made so as to avoid a double registration requirement. Almost all consultees agreed. The response of the Law Society of Scotland, which was echoed by Brodies, was representative: "[We are] in favour of avoiding having to register the same security in two separate registers. [We do], however, see the benefit in such security appearing in both registers. A collaborative approach between the various registers would presumably assist here." The WS Society said: "We are not convinced it is anything other than a backward step to require in future a search in multiple registers instead of a single register where one is dealing with a company or LLP."

36.14 If a section 893 order were made registration would be in the specialist register (for present purposes the RSP) and the information would then be transmitted to the Companies Register. Dr Hamish Patrick, however, argued for the reverse, whereby a statutory pledge granted by a company would be registered in the Companies Register and the information would then be relayed to the RSP.

The way forward

36.15 After considering the responses of consultees we reflected on the way forward, particularly in the light of the absence of any section 893 orders to date. We engaged in discussions with Companies House, DBIS (as it was then called) and Registers of Scotland. In this regard we considered a number of different options. Our starting point was a policy that statutory pledges granted by any type of person would be registrable in the RSP. In the case of companies we then needed to take account of the company charges registration scheme. We identified three options in relation to which DBIS, on behalf of Companies House, and Registers of Scotland gave us their views.

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[24] Department for Business, Innovation and Skills Consultation Paper, *Registration of charges created by companies and limited liability partnerships* (2010) 46.
[25] Discussion Paper, para 20.47.

Double registration

36.16 The first option was double registration. This is unattractive because it is cumbersome. It also involves the payment of two registration fees. But the latter is probably not a particularly strong argument, because the cost of information-sharing arrangements would inevitably lead to a higher fee for the one registration in the RSP.

36.17 As Part 25 of the Companies Act 2006 currently stands there is also an issue in that the usual rule for the 21-day period is that it runs from the day of delivery of the security document to the creditor. This leads to the possibility of a creditor complying with this timescale but then forgetting to register in the RSP. The Companies Register would then be unreliable. In contrast, the rule for standard securities is that the 21 days run from the day of registration in the Land Register. UK subordinate legislation would be needed to address this. There would also be benefit in such legislation making it clear that the current exclusion of the requirement to register a "pledge"[26] does not include the new statutory pledge. These issues aside, the first option could proceed without any UK legislation. It also had the support of DBIS in correspondence with us.

Section 893 order

36.18 The second option was an order under section 893 of the 2006 Act. As we have seen, it had the support of most of our consultees. It would avoid the need for double registration. In discussions with us, it also remained "on balance" the preferred option of Registers of Scotland. In contrast, in relation to the first option, Registers of Scotland said that "double registration risks becoming bureaucratic and cumbersome". An order under section 893 would require DBIS support and it had to be satisfied that its four criteria set out above[27] had been met.[28] DBIS also advised us that no money was available from Companies House to meet the costs of establishing the new information-sharing arrangements.

36.19 A further issue with a section 893 order relates to how registration in the RSP would normally work. In the preceding chapters we recommended a registration scheme similar to that in UCC–9/PPSA jurisdictions, namely one of electronic filing with no checks being made by the Keeper. This allows also for quick and inexpensive registration. In contrast, when a charge is registered in the Companies Register, it is checked by Companies House staff[29] before it is entered on the register. A section 893 order would require this approach to be taken at the RSP where the provider of a statutory pledge is a company. Such an approach would be possible, although it would conceivably require legislative amendment to our

[26] Companies Act 2006 s 859(7)(b).
[27] See para 36.12 above.
[28] We note that in the different context of DBEIS, *A Register of Beneficial Owners of Overseas Companies and other Legal Entities: Call for evidence on a register showing who owns and controls overseas legal entities that own UK property or participate in UK government procurement* (2017) para 17 it is stated: "It is important to both the UK and Scottish Governments that no companies will be required to report their information twice under the linked proposals [in relation to ownership and control of property]."
[29] Note L Gullifer and M Raczynska, "The English Law of Personal Property Security: Under-refomed?" in Gullifer and Akseli (eds), *Secured Transactions Law Reform* 271 at 282.

recommended scheme in relation to companies by the UK Parliament, given that the law of business associations is currently reserved.[30]

Joint filing service

36.20 The third option arose out of discussions with Companies House. It alerted us to the joint electronic filing service for company accounts whereby information filed once is transmitted to both Companies House and HMRC.[31] We considered whether there would be benefit in recommending a joint electronic filing service for statutory pledges granted by companies whereby there was a single portal managed by Companies House and Registers of Scotland. The advantages of this would be one filing only and Companies House would be able to check security documents under its usual procedures, rather than rely on Registers of Scotland doing this, which is what would require to happen for a section 893 order to be made. Clearly, however, there would be set-up and running costs in relation to such a system and DBIS advised us that there would be no funding available from Companies House. Registers of Scotland were of the view that a joint filing system would be costlier than the second option of a section 893 order.

36.21 There would be other challenges with this option. It would not be possible always to use the company charges registration form (currently form MR01) as it does not have a box for unique identification numbers, such as vehicle identification numbers (VINs). We recommend elsewhere that the RSP should be searchable by reference to such numbers.[32] Implementation of the joint filing scheme would require legislation, in contrast to the second option where section 893 is already on the statute book. We are of the view that the Registrar of Companies already has the power to allow statutory pledges to be registered by means of a new electronic registration system.[33] But we think that further UK legislation would be required. Under this option, there would require to be legislative provisions which would apply specifically to companies. For example, it would have to be provided that it would be possible to register statutory pledges granted by companies in the RSP by using the new joint online filing service. As discussed elsewhere,[34] company law is in general a reserved matter and so any legislation would need to be enacted by the UK Parliament.

36.22 Given the lack of support from two key stakeholders – DBIS/Companies House and Registers of Scotland – we do not consider the joint filing scheme option as viable. This leaves the double registration and section 893 order options. Before reaching a conclusion in relation to these, we considered other options. Two of these merit discussion here.

Reverse section 893 order

36.23 The first of these is that championed by Dr Patrick in his consultation response. It can be termed in shorthand a "reverse section 893 order". Under this option creditors would be able to give effect to statutory pledges granted by *companies* by registering at a single registration point: the Companies Register. This would involve setting up information-sharing arrangements between Companies House and Registers of Scotland. When a

[30] See para 1.43 above.
[31] Her Majesty's Revenue and Customs.
[32] See para 34.5 above.
[33] Companies Act 2006 s 1068. See also the rule making power under s 1117 of the same Act.
[34] See paras 1.43 above.

statutory pledge was registered in the Companies Register, information about the security right would then be transmitted electronically to the RSP. As a result of these information-sharing arrangements, the RSP would contain every statutory pledge (apart from those over financial instruments perfected by possession or control).[35] In addition, the implementation of the information-sharing arrangements would allow statutory pledges to be treated as if registered in the RSP on the date of registration in the Companies Register. This would mean that a statutory pledge granted by a company over current and identifiable assets would be created as a real right on the date of registration in the Companies Register.

36.24 In our view, the Secretary of State would not be able to implement this option by making a section 893 order. New amending UK legislation would be required, given that company law is reserved.[36] We note also that the Register of Floating Charges Technical Working Group, which was set up by the Scottish Government to consider implementation of Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007,[37] looked at a similar option and rejected it for various reasons, including concerns about issues of liability and powers of the two registration agencies in relation to the creation of the security being dependent on transmission of information from Companies House to Registers of Scotland.[38] There would also be similar costs concerns as with the section 893 order and joint filing service options. We therefore do not recommend this option.

Registration only in the Companies Register

36.25 The remaining option does not involve information sharing and its associated costs, and for these reasons is initially very attractive.[39] Where a company granted a statutory pledge it would be registered in the Companies Register alone and therefore only one registration fee would have to be paid. Where a non-company, such as a sole trader or partnership, granted a statutory pledge it would be registered in the RSP. This would depart from the original proposed scheme that the RSP would contain all statutory pledges. Under this option statutory pledges would be fragmented across the Companies Register and the RSP. The RSP would therefore be incomplete.[40] It would also be somewhat anomalous to have the same type of security right created in different ways by different types of debtor.

36.26 There is another difficulty. The Companies Register can be searched by company but not by assets. As we noted above,[41] we recommend elsewhere that the RSP should be searchable by reference to unique identification numbers. Thus creditors wishing to take statutory pledges from companies, for example, over motor vehicles and have the VIN(s) registered would have a problem. This could be fixed by permitting the registration of such statutory pledges in the RSP, even although granted by companies. But the result would be (i) statutory pledges granted by non-companies; and (ii) statutory pledges granted by companies over property with unique identification numbers.

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[35] See Chapter 37 below.
[36] This might be only subordinate legislation made under the Companies Act 2006 s 894.
[37] See para 18.25 above.
[38] See Register of Floating Charges Technical Working Group: Report to Scottish Government (2011) para 5.1.4, available at http://www.scotland.gov.uk/resource/doc/254430/0121799.pdf.
[39] See eg J Hardman, "Some Legal Determinants of External Finance in Scotland: A Response to Lord Hodge" (2017) 21 EdinLR 30 at 47–48.
[40] Although given the Financial Collateral Arrangements (No. 2) Regulations 2003 it cannot be complete. See Chapter 37 below.
[41] See para 36.21 above.

36.27 The implementation of this option would require company-specific rules. The legislation would have to provide that statutory pledges granted by companies over assets (other than prescribed assets with unique identification numbers) would only require registration in the Companies Register. It would be registration in that register which would be constitutive of the statutory pledge. For existing security rights granted by companies, registration in the Companies Register is not constitutive; it is necessary only for effectiveness in insolvency and against other creditors.[42] As these legislative provisions would deal specifically with statutory pledges granted by companies and provide a new function for registration in the Companies Register we take the view that UK legislation would be required to implement this option. This would also mean the new law being in two different places, namely in an Act of the Scottish Parliament and in UK legislation,[43] which would not be user-friendly. It would also be more difficult to secure resources at DBEIS and legislative time at Westminster to effect this, given the other priorities which exist at UK level not least the withdrawal from the European Union. While therefore the option of registration in the Companies Register only is attractive at first sight, on closer examination it has significant difficulties and therefore we do not recommend it.

Conclusion

36.28 Having reviewed the various options and discussed them at length with our advisory group, we have concluded that double registration offers the most pragmatic solution as it does not require the funding that would be necessary to set up information-sharing arrangements. Further, it does not require legislation at UK level. Creditors are experienced at registering twice, because they need to do so for other securities, such as standard securities. Nevertheless, we consider that the possibility of a section 893 order should be kept under review as in the longer term it remains desirable to require only a single filing. We recommend that:

193. A statutory pledge granted by a company should be registered in both the Register of Statutory Pledges and the Companies Register, but the possibility of an order being made under the Companies Act 2006 section 893 should be kept under review.

[42] See para 36.8 above. Of course an alternative would be to put the statutory pledge on the same footing as a floating charge and not make registration constitutive so that there is an "invisibility period". We are unwilling to so recommend. See para 36.7 above.

[43] Perhaps an Act of the Scottish Parliament plus an order under section 104 of the Scotland Act 1998.

Chapter 37 Financial collateral

Introduction

37.1 In Chapter 14 above we set out the special rules in relation to financial collateral. These originate from the Financial Collateral Directive of 2002 (as amended),[1] which was implemented in the UK by the Financial Collateral Arrangements (No. 2) Regulations 2003 ("FCARs").[2]

37.2 Given our earlier recommendation on limiting the scope of the statutory pledge to financial instruments, it is in relation to that type of property that we now need to consider the extent to which any variations to our general scheme are required to comply with the special rules on financial collateral.

Pledge of financial instruments

Creation of statutory pledge

37.3 We recommended earlier that registration should be a requirement for the creation of a statutory pledge.[3] We recommended also as regards incorporeal moveable property that the statutory pledge should be restricted to financial instruments and intellectual property. Clearly, only the former come within the scope of the Directive. Where a statutory pledge is granted in respect of a financial instrument and the requisite possession or control is achieved we consider now that the statutory pledge could qualify as a security financial collateral arrangement (SFCA).[4] In such circumstances, given the terms of the Directive, we do not think that registration in the RSP can be insisted upon. Given, however, the opaque terms of the Directive, in particular as regards possession or control, we consider that parties would wish to retain the option of registration in the RSP as this would give them certainty as to creation. If the SFCA route, as opposed to the registration route, were chosen it would still nevertheless be necessary for the financial instrument to be the property of the provider and to be identifiable as property to which the constitutive document relates.

37.4 Where a statutory pledge is created as an SFCA it is also necessary for the usual requirement for its constitutive document to be executed or signed electronically to be disapplied. The statutory pledge need only be evidenced in writing transcribed by electronic or other means in a durable medium, or as sounds recorded in such a medium.

37.5 We therefore recommend:

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[1] Directive 2002/47/EC.
[2] Financial Collateral Arrangements (No. 2) Regulations 2003 (SI 2003/3226) as amended by the Financial Markets and Insolvency (Settlement Finality and Financial Collateral Arrangements) (Amendment) Regulations 2010 (SI 2010/2993).
[3] See para 23.19 above.
[4] This departs from the view that we took in the Discussion Paper, para 2.25, which was that without registration the collateral provider would not have "control". It is impossible to be certain, however, but we have now, following advice from our advisory group, decided to take a cautious approach and assume that the Directive would apply.

194. The creation of a statutory pledge over a financial instrument should require either:

(a) registration in the Register of Statutory Pledges and compliance with the ordinary rules for creation of statutory pledges, or

(b) in a case where a constitutive document or amendment document evidences a security financial collateral arrangement in respect of the instrument, the satisfaction of the following criteria:

(i) the financial instrument to be the property of the provider,

(ii) the financial instrument to have come into the possession of, or under the control of, the collateral-taker or a person acting on the collateral-taker's behalf, and

(iii) identification of the financial instrument as one to which the constitutive document or amendment document relates.

(Draft Bill, s 50(1)–(3) & (6))

195. Where a statutory pledge over a financial instrument is created without registration:

(a) there should be no requirement for it to be executed or signed electronically, and

(b) the constitutive document and any amendment document may be evidenced by writing transcribed by electronic or other means in a durable medium, or as sounds recorded in such a medium.

(Draft Bill, s 50(4) to (6))

Assignation of statutory pledge

37.6 We recommended earlier that the assignation of a statutory pledge should require an assignation document executed or authenticated by the secured creditor.[5] Where a statutory pledge is an SFCA we consider that the policy aim of the Directive to reduce formalities should be implemented by removing the need for execution or authentication. Instead an evidenced agreement between the collateral-taker (secured creditor) and the assignee should suffice. In line with the position for creation of a statutory pledge, as an SFCA the agreement could be evidenced in writing transcribed by electronic or other means in a durable medium, or in sounds recorded in such a medium. We recommend:

196. Where a statutory pledge over a financial instrument is created without registration:

[5] See para 23.42 above.

(a) it may be assigned by an evidenced agreement between the collateral-taker and the assignee, and

(b) that agreement may be evidenced in writing transcribed by electronic or other means in a durable medium, or in sounds recorded in such a medium.

(Draft Bill, ss 59(3) and 63)

Amendment of statutory pledge

37.7 We also recommended earlier that the amendment of a statutory pledge should normally require a document executed or authenticated by the provider and secured creditor.[6] Where a statutory pledge is an SFCA, as for assignation we consider that the policy aim of the Directive to reduce formalities should be implemented by removing the requirement for execution or authentication. An evidenced agreement between the collateral-taker (secured creditor) and the collateral-provider (provider) should be competent. Once again this could be evidenced in writing transcribed by electronic or other means in a durable medium, or in sounds recorded in such a medium. We recommend:

197. Where a statutory pledge over a financial instrument is created without registration:

(a) it may be amended by an evidenced agreement between the collateral-taker and the provider, and

(b) that agreement may be evidenced in writing transcribed by electronic or other means in a durable medium, or in sounds recorded in such a medium.

(Draft Bill, ss 60(8) and 63)

Extinction of statutory pledge

37.8 Under our recommendation above, a statutory pledge which qualifies as an SFCA can be created if (a) the SFCA requirements are satisfied; or (b) if there is registration in the RSP. For (a) to be satisfied the secured creditor (collateral-taker) would require to have possession or control of the financial instrument.

37.9 Where a statutory pledge has been created as an SFCA without registration clearly it does not make sense for any action to be taken in the RSP. Instead either the statutory pledge could be extinguished by the collateral-taker relinquishing possession or control. Alternatively, we consider that it should be possible to restrict or discharge the security by an evidenced statement of the collateral-taker. In line with the provisions on creation of an SFCA, the statement could be evidenced by writing transcribed by electronic or other means in a durable medium or sounds recorded in such a medium.

37.10 We therefore recommend:

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[6] See paras 23.33–23.40 above. But an amendment adding property should only need execution or authentication by the provider.

198. (a) A statutory pledge created as a security financial collateral arrangement without registration in the Register of Statutory Pledges should be:

(i) extinguished in relation to the financial instrument over which the pledge is created on the financial instrument ceasing to be in the possession, or under the control, of the collateral-taker or of a person acting on behalf of the collateral-taker, or

(ii) restricted to only part of the encumbered property by means of an evidenced statement of the collateral-taker.

(b) Such a statement may be evidenced in writing transcribed by electronic or other means in a durable medium, or sounds recorded in such a medium.

(Draft Bill, ss 62 and 63)

Rights of substitution and withdrawal

37.11 The definition of an SFCA in the FCARs enables the parties to agree that the collateral-provider can substitute financial collateral of the same or greater value or withdraw excess financial collateral without losing possession or control of the collateral.[7] Under English law it is very likely that such an agreement would make the SFCA a floating charge.[8] Given that a statutory pledge is a fixed security we consider therefore that special rules in relation to substitution and withdrawal are not relevant. As we have noted elsewhere, the fixed/floating distinction is a matter of corporate insolvency law where the relevant legislation is the Insolvency Act 1986.[9] It is possible that future developments, for example in English case law or in UK legislation, may make it clear that rights of substitution or withdrawal do not prevent an SFCA being a fixed security. If that happens then the statutory pledges legislation could be amended.

Ranking

37.12 The ranking of a statutory pledge over a financial instrument created as an SFCA would be subject to the same general ranking rule which we recommend above.[10] Thus the priority point would be creation. It would seem unlikely that there could be two pledges created as SFCAs over the same instrument because of the need for possession or control. Thus if Bank A has possession or control this would preclude Bank B having possession or control. On the other hand it is possible to envisage Bank A having a statutory pledge by possession or control and Bank B having a statutory pledge by registration.

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[7] FCARs reg 3(1).
[8] See Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* para 3.39 and Yeowart and Parsons, *The Law of Financial Collateral* paras 8.13 and 8.82–8.99.
[9] See para 20.1 above.
[10] See paras 26.1–26.10 above.

Enforcement

37.13 Elsewhere we make recommendations on enforcement of pledges.[11] But the Directive and FCARs make special provision for rights exercisable by the collateral-taker in the case of an SFCA, namely rights of use and appropriation.[12] Thus an SFCA may allow the collateral-taker to use and dispose of the collateral provided that it is replaced with equivalent collateral on or before the due date for the performance of the relevant financial obligations which are covered by the SFCA.[13] Alternatively, if the SFCA permits this, the used or appropriated collateral can be set off against or applied in the discharge of the relevant financial obligations.[14] Where the SFCA permits appropriation no foreclosure order is required from a court.[15] But the collateral must be valued in accordance with the terms of the SFCA and in a commercially reasonable manner.[16] If the value exceeds the amount of the relevant financial obligations under the SFCA then the collateral-taker must account to the collateral provider for the difference. If the value is less than these obligations then the collateral provider remains liable to the collateral-taker for the shortfall.[17]

37.14 Where a statutory pledge falls within the definition of an SFCA the special rights of use and appropriation require to be available. We recommend:

199. Nothing in the enforcement rules for pledge should be taken to derogate from such rights as a secured creditor may have by virtue of Part 4 of the Financial Collateral Arrangements (No. 2) Regulations 2003 (right of use and appropriation).

(Draft Bill, s 84)

[11] See Chapters 27 and 28 above.
[12] Directive, Arts 4 and 5; FCARs Part 4. See Beale, Bridge, Gullifer and Lomnicka, *The Law of Security and Title-Based Financing* paras 3.09–3.10. In Scotland a right of use is also conferred in TTFCAs.
[13] Directive, Art 5(1) and (2); FCARs reg 16(1) and (2).
[14] Directive, Art 5(2); FCARs reg 16(2).
[15] FCARs reg 17(1).
[16] Directive, Art 4(2); FCARs reg 18(1).
[17] Directive, Art 4(1); FCARs reg 18(2).

Chapter 38 Floating charges and agricultural charges

Introduction

38.1 This chapter addresses reform in relation to floating charges and agricultural charges. We have a limited amount to say about floating charges. Earlier in this Report we considered Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007, which makes provision for substantial reform of the law of floating charges in Scotland, but has not been brought into force.[1] We also discussed the floating charge in Chapter 20 where we set out our recommendation to depart from an aspect of the scheme proposed in the Discussion Paper and not to take forward the idea of a "floating lien". We note there the support from a significant number of our consultees for retention of the floating charge. Here we consider the reform questions raised in the Discussion Paper in relation to this type of security right.

Floating charges, sole traders and companies

38.2 The reforms proposed by the Murray Report[2] included a recommendation that sole traders and ordinary partnerships should be able to grant floating charges, but only over their moveable assets. The aim was to make the law on rights in security less restrictive for these forms of trading entities. In the Discussion Paper and now here we have taken a different approach, namely the introduction of the statutory pledge. We therefore asked consultees whether they agreed that the recommendation of the Murray Report that sole traders and ordinary partnerships should be able to grant floating charges, should not now be taken forward.

38.3 There was a division of opinion among consultees. Around half of those who responded to this question agreed. Brodies stated: "Subject to an adequate form of fixed security over moveable property being available to sole traders and ordinary partnerships we do not see a need for the extension of floating charges to these groups." Of those who did not say that they agreed, the strength of feeling varied. Dr Hamish Patrick supported the introduction of floating charges for partnerships, but "probably" not for sole traders. The Judges of the Court of Session said; "Whatever the defects of the floating charge, it might be worth giving greater consideration to the Murray Report proposal as an alternative to the creation of a wholly new security over moveable property." The Law Society of Scotland and some law firm consultees supported the Murray Report recommendation.

38.4 We consider that one of the lessons of Part 2 of the 2007 Act is that any significant reform of floating charges on a Scotland-only basis is likely to encounter opposition. We are also very much aware that the law of business associations is reserved to the UK Parliament,[3] albeit floating charges law is devolved.[4] Moreover, support for reform from our

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[1] See paras 18.23–18.25 and 18.41–18.43 above.
[2] See paras 18.18–18.22 and 18.38–18.40 above.
[3] Scotland Act 1998 Sch 5 Part II Head C1. See also Law Commission and Scottish Law Commission, Partnership Law (Law Com No 283, Scot Law Com No 192, 2003).
[4] Scotland Act 1998 Sch 5 Part II Head C2.

consultees was limited and we do not think that the modification of our scheme to abandon the floating lien justifies the further rolling-out of the floating charge.[5] Finally, any legislation permitting sole traders and partnerships to grant floating charges could be complex in relation to covering the possibility of business continuity when, for example, a sole trader formed a partnership. We conclude that:

200. The recommendation of the Murray Report that sole traders and ordinary partnerships should be able to grant floating charges should not now be taken forward.

Floating charges: the land issue

38.5 In the Discussion Paper we noted that there is a case for providing that floating charges granted in future should not cover immoveable/heritable property.[6] The equivalent security rights under UCC–9 and the PPSAs, as well as German law,[7] cover moveables only. In Scotland, the floating charge has been particularly controversial in relation to land.[8] The Murray Report asked consultees whether they thought that in future floating charges should not be capable of covering land. In the Discussion Paper we did the same.

38.6 A clear majority of consultees including Chris Dun, the Faculty of Advocates, Dr Hamish Patrick, the Law Society of Scotland and several law firms opposed the suggestion that floating charges should be restricted to moveable property. Once again there is clearly a background here of a desire for floating charges in Scotland to have the same scope as those in England. We therefore recommend that:

201. Floating charges should continue to be capable of encumbering immoveable/heritable property.

The ranking of floating charges

38.7 It is common in floating charges to have a "negative pledge" clause, forbidding the creation of subsequent fixed securities. By statute in Scotland a registered floating charge with such a clause will rank above any such subsequent fixed security.[9] In England the position at the time that the Discussion Paper was published was that negative pledge clauses would only affect subsequent secured creditors if they were actually aware of them. Such clauses did not appear on the Companies Register. The Discussion Paper noted proposals to alter English law so that registration would be possible and thus subsequent chargees could be regarded as having constructive notice of the negative pledge clause. This would mean that they would rank after the floating charge.[10] But at that time, such a reform was by no means certain. Given the proposal that the new security could apply to after-acquired assets and some ranking problems affecting floating charges, we asked consultees whether the Scottish ranking rules should be reformed to bring them into line with those in England and Wales.

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[5] See Chapter 20 above.
[6] Discussion Paper, para 9.17.
[7] The *Sicherungsübereignung* and the *Sicherungsabtretung.*
[8] In particular in *Sharp v Thomson* 1997 SC (HL) 66, on which see Scottish Law Commission, Report on *Sharp v Thomson* (Scot Law Com No 208, 2007).
[9] Companies Act 1985 s 464(1A). See *AIB Finance plc v Bank of Scotland* 1993 SC 588.
[10] Discussion Paper, para 22.32.

38.8 There was a mixed response from consultees. Several, including Dr Ross Anderson, David Cabrelli, Chris Dun and Jim McLean favoured such a change. Others, including Dr Hamish Patrick, the Law Society of Scotland and several law firms, did not.

38.9 In the meantime there has been reform in England and since 1 April 2013 it has been possible to register negative pledge clauses in the Companies Register.[11] The effect of this is said to be that subsequent chargees will have constructive notice and therefore rank after the floating charge.[12] We therefore do not consider that it makes sense for the Scottish rules to be brought into step with the former English rules. We recommend that:

202. The ranking rules of Scottish floating charges in relation to negative pledge clauses should not be reformed.

Floating charges and "effectually executed diligence"

38.10 A floating charge is subject to "effectually executed diligence".[13] In *Lord Advocate v Royal Bank of Scotland*[14] it was held that where (i) a floating charge was constituted; (ii) another creditor arrested; and (iii) the charge crystallised without an action of furthcoming having been raised, the arrestment was not "effectually executed". This decision has been widely criticised.[15] Subsequent research using Hansard has also revealed that the intention of Parliament had been that in such a case the arrestment was to prevail.[16] In the Discussion Paper, we proposed that the relevant statutory provisions should be amended so as to ensure that the original intention of the legislation is given effect to. Most consultees who responded to the question agreed.

38.11 There has since been a major development. In 2017 a five-judge bench of the Inner House in *MacMillan v T Leith Developments Ltd (in receivership and liquidation)*[17] overruled *Lord Advocate v Royal Bank of Scotland* on the basis that the court in the earlier case had misinterpreted the relevant statutory provision. In the words of Lord President Carloway:

> "The problem with the reasoning of the majority and the Lord Ordinary in *Lord Advocate v Royal Bank of Scotland* is that it effectively drives a coach-and-four through the common law of diligence in circumstances in which the statutory wording was, as Lord Johnston described it, intended to be a saving provision designed to achieve the opposite effect . . . The whole purpose of [the relevant provisions] was to preserve the rights of diligence holders notwithstanding the effect of the charge's crystallisation."[18]

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[11] Companies Act 2006 s 859D(2)(c).
[12] See Calnan, *Taking Security* para 7.299. At para 7.300 he writes: "This is a desirable result. There is much to be said for the view that all charges – whether fixed or floating – should rank in order of creation unless the parties otherwise agree." This in fact is what the Bankruptcy and Diligence etc. (Scotland) Act 2007 Part 2 provides, although as mentioned above the relevant provisions have not been commenced.
[13] Companies Act 1985 s 463; Insolvency Act 1986 ss 55 and 60; Bankruptcy and Diligence etc. (Scotland) Act 2007 s 45.
[14] 1977 SC 155, interpreting the pre-1985 Act legislation, the Companies (Floating Charges and Receivers) (Scotland) Act 1972, which was in similar terms.
[15] See eg W A Wilson, "Effectually executed diligence" 1978 Juridical Review 253; A J Sim, "The receiver and effectually executed diligence" 1984 SLT (News) 25 and G L Gretton, "Receivers and arresters" 1984 SLT (News) 177.
[16] See generally S Wortley, "Squaring the Circle: Revisiting the Receiver and 'Effectually Executed Diligence'" 2000 Juridical Review 325.
[17] [2017] CSIH 23.
[18] [2017] CSIH 23 at para 57.

38.12 The decision was not appealed to the Supreme Court. We note the risk mentioned by Scott Wortley in his article on this issue that the approach now taken by the Inner House in *MacMillan* could lead to floating charge holders putting companies into liquidation so that the 60 day equalisation of diligence rule will negate the preference achieved by the creditor who has carried out diligence.[19] We note also that Part 2 of the Bankruptcy and Diligence etc. (Scotland) Act 2007 did not address the issue, which suggests again that it is a difficult one. While we make no formal recommendation here, we think that the matter may benefit from review as and when future reform of corporate insolvency law is considered.

Agricultural charges

38.13 The agricultural charge is a security which was introduced by the Agricultural Credits (Scotland) Act 1929. This followed similar legislation in England and Wales, the Agricultural Credits Act 1928. It can only be granted by agricultural co-operatives in favour of banks.[20] The effect is similar to a floating charge, though one important difference is that whereas a floating charge can cover property of every type, the agricultural charge is limited to "stocks of merchandise".[21] Under the legislation as passed, agricultural charges had to be registered in a register maintained by the Assistant Registrar of Friendly Societies for Scotland.[22] This requirement was repealed by the Financial Services and Markets Act 2000 (Consequential Amendments and Repeals) Order 2001.[23] Registration is still required for agricultural charges in England and Wales under the 1928 Act.[24] Agricultural charges appear no longer to be enforceable outside insolvency since the 1929 Act provides only for enforcement by sequestration for rent,[25] a process that no longer exists.[26] Placing the debtor into insolvency seems a disproportionate means of enforcement.

38.14 In the Discussion Paper we stated our impression that agricultural charges are rarely used in practice.[27] We have since had that this confirmed by the Scottish Agricultural Organisation Society Ltd,[28] as well as by the Law Society of Scotland in its response to our draft Bill consultation of July 2017. In practice co-operatives grant floating charges rather than agricultural charges. They have power to do this, formerly as industrial and provident societies, and now as registered societies under the Co-operative and Community Benefit Societies Act 2014.[29]

38.15 As a result of our scheme to introduce a new security over moveable property, we proposed in the Discussion Paper that the 1929 Act should be repealed. All our consultees who responded to this proposal agreed. While we now recommend that the statutory pledge

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[19] Wortley, "Squaring the Circle" at 341 ff.
[20] 1929 Act s 5. For the definition of "bank" for this purpose, see the Financial Services and Markets Act 2000 (Consequential Amendments and Repeals) Order 2001 (SI 2001/3649) art 217.
[21] 1929 Act s 5.
[22] 1929 Act s 8.
[23] SI 2001/3649 art 216. The 2000 Act s 335 enabled the functions of the Registry of Friendly Societies to be transferred to the Financial Services Authority and for the former to be closed. This happened on 1 December 2001 by virtue of the Financial Services and Markets Act 2000 (Mutual Societies) Order 2001 (SI 2001/2617). Agricultural co-operatives are now regulated by the Financial Conduct Authority in terms of the Co-operative and Community Benefit Societies Act 2014.
[24] See Law Com Report No 369 para 4.36. The register is based in Plymouth and maintained by the Land Registry.
[25] 1929 Act s 6(1).
[26] Bankruptcy and Diligence etc. (Scotland) Act 2007 s 208.
[27] Discussion Paper, para 16.80.
[28] See http://www.saos.coop/.
[29] See the Co-operative and Community Benefit Societies Act 2014 ss 62–64.

should be fixed only and not floating, we do not consider that this makes a difference. The information which we now have is that the agricultural charge is redundant in practice in Scotland because of the floating charge. We therefore consider that the future grant of agricultural charges should not be possible.[30] Although, agricultural co-operatives are business associations and certain aspects of that area of law are reserved to the UK Parliament,[31] rights in security are not and are therefore in our view within devolved legislative competence. We recommend:

203. It should no longer be competent for agricultural charges to be created.

(Draft Bill, s 115)

[30] Rather than to repeal the Act, given that some agricultural charges could be extant.
[31] See para 1.43 above.

Chapter 39 International private law

Introduction

39.1 In Chapter 15 above we noted that some consultees questioned the approach taken in the Discussion Paper that international private law was outwith our scope. We sought to consider the subject in relation to assignation. We attempt here to outline the various international private law issues which arise from the two security strands of the project: (i) security over incorporeal moveable property; and (ii) security over corporeal moveable property. We consider also jurisdiction.

Applicable law: security over incorporeal moveable property

39.2 Article 14(3) of the Rome I Regulation specifically states that transfers of claims by way of security are included within its scope.[1] The discussion in Chapter 15 above therefore applies to assignations in security just as much as to outright transfers.

39.3 Our recommendations would enable a true security right to be granted over two types of incorporeal moveable property, namely financial instruments and intellectual property, by means of the statutory pledge, as opposed to the conventional route of assignation with a personal obligation to re-transfer the property on repayment of the debt due. Article 14 of the Rome I Regulation clearly does not apply to intellectual property. It is also unlikely that it applies to shares, but the position as regards other financial instruments is unclear.[2]

39.4 In relation to intellectual property there are particular issues. Such rights apply the *lex situs* conflict of laws rule. But the current UK intellectual property legislation does not attribute intellectual property to a particular legal system. Moreover, for registered rights there is only a single UK-wide register. The conflict of laws rule is therefore ineffective as it results in pointing simultaneously to both English and Scots law. As was noted in the Discussion Paper, there is no clear answer on how to fix this issue although the predominant view seems to be that the *lex situs* of intellectual property, for the purposes of security rights granted over them, is determined by the domicile of the holder of the intellectual property.[3] Further, the law on intellectual property is generally reserved to the UK Parliament and therefore it would not be competent for our draft Bill to make provision on this.[4]

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[1] For background see M McParland, *The Rome I Regulation on the Law Applicable to Contractual Obligations* paras 18.14–18.21.

[2] See McParland, *The Rome I Regulation on the Law Applicable to Contractual Obligations* paras 18.13 and 18.20. See also the special rules for book entries security collateral under reg 19 of the Financial Collateral Arrangements (No. 2) Regulations 2003 (SI 2003/3226).

[3] See Discussion Paper, para 7.20 and fn 14 referring to Lord Evershed's statement that "[a]n English patent is a species of English property of the nature of a chose in action and peculiar in character" in *British Nylon Spinners Ltd v Imperial Chemical Industries Ltd* [1953] Ch 19 at 26.

[4] See para 1.47 above.

Applicable law: security over corporeal moveable property

39.5 Transactions involving corporeal moveable property present fewer issues than with incorporeals, mainly due to the fact that their physical form makes application of the *lex situs* rule much easier. The precise rule for transactions involving corporeal moveable property is that the law applicable is that of the location of the property at the time of the relevant dealing.[5]

39.6 Once a security right has been created over corporeal moveable property and the property has been removed to a foreign jurisdiction, the recognition of that security right is a matter for the law of that foreign jurisdiction. Professor Carruthers explains:

> "As a general rule, removal of an object across state borders should not undermine, per se, pre-existing, or vested, rights in the object, but this rule pertains only so long as there are no further dealings with the object in the new *situs*. Following removal of the object to a new *situs*, the law of the new *situs* will determine the existence and priority of interests in the object. Though rare, it is possible that, indirectly, mere removal of an object to a new *situs* may adversely affect 'vested' rights insofar as there exist difficulties of transposition of legal right or entitlement."[6]

39.7 Thus, where a statutory pledge is granted over a car in Scotland and the car is driven to France, the security would remain valid as far as Scots law is concerned, but it would then be a matter for the French courts to decide whether or not to recognise the foreign security. This would include determining whether a subsequent purchaser or acquirer of a security right over the property would take subject to the Scottish security right. If the car was subsequently driven back to Scotland without any further transaction, there would be no effect on the security right.

39.8 This principle applies equally in Scotland where the recognition of foreign security rights is a matter for the Scottish courts. There is little authority in this area, but the case of *Hammer and Sohne v HWT Realisations Ltd*[7] provides some guidance. It involved a foreign retention of title clause in a contract for jewellery received by a Glasgow-based company. Sheriff Jardine held that the issue of whether such a clause (and security rights in general) should be treated as a true security right was a matter for the new *lex situs* to determine. He concluded that since the contract was essentially one for the creation of a security right without possession, it was ineffective to retain the seller's ownership of the goods.

39.9 Peculiarly, this meant characterising the issue as one pertaining to security rights, only to hold that no recognised security right existed.[8] Sheriff Jardine's judgment signifies that the Scottish courts will not recognise a foreign right in security which was valid under the *lex situs* when created, if no comparable security right exists under Scots law. This is particularly problematic since most other jurisdictions recognise some form of non-possessory security over corporeal moveable property. There are therefore economic implications for foreign companies considering doing business in Scotland.

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[5] *Inglis v Robertson & Baxter* (1898) 25 R (HL) 70 per Lord Watson at 73; *Armour v Thyssen Edelstahlwerke AG* 1986 SLT 452 per Lord Mayfield at 455.
[6] J M Carruthers, *The Transfer of Property in the Conflict of Laws* (2005) para 3.45.
[7] 1985 SLT (Sh Ct) 21.
[8] For criticism of the case, see D Gordon, "Scotland: Romalpa clauses: some reservations on choice of law" (1986) 7 Comp Law 125 at 126; H Patrick, "Romalpa: the international dimension" 1986 SLT (News) 265 at 270.

39.10 Under our recommendations, however, a foreign form of registered non-possessory security right would be recognisable under Scots law as comparable to the new statutory pledge. There is therefore a strong economic argument for introducing the statutory pledge in order to remove any barriers to cross-border transactions involving foreign companies transacting in Scotland.

39.11 The *lex situs* rule for issues pertaining to security interests creates some concerns in relation to highly mobile corporeal moveable property, particularly with aircraft which may not have a real connection with any location since they are almost constantly moving. However, as we have seen, aircraft have their own specialised security regime under the Mortgaging of Aircraft Order 1972 and the Cape Town Convention, and are effectively excluded from being the subject of a statutory pledge.[9]

39.12 At a more general level, we think that it would be undesirable to depart from the *lex situs* rule for security rights involving corporeal moveable property without a review of the rule in the wider context of property law. We are also conscious that the *lex situs* remains the generally accepted rule internationally and therefore that reform at an international level is more appropriate. We have therefore concluded that we should not review the rule as part of this project.

Jurisdiction

39.13 We refer to our discussion of this subject in relation to assignation,[10] where we concluded that the matter should be left to the existing rules. We note, however, that jurisdiction was considered in clause 30 of the draft Bill attached to the Murray Report,[11] which defined "court" for its purposes as:

> "(a) where the granter of a floating charge or, as the case may be, moveable security is domiciled in Scotland, the Court of Session or the sheriff within whose sheriffdom the granter is domiciled; or
>
> (b) where such granter is not so domiciled but the property which is subject to the charge or security is situated in Scotland, the Court of Session or sheriff within whose sheriffdom such property is situated;
>
> (c) where such granter is not so domiciled but the incorporeal moveable property which is subject to the charge or security is governed by the law of Scotland, the Court of Session".

39.14 It is unclear why such a clause was included. The Report itself is silent on the issue of jurisdiction and accordingly there is no discussion of the existing rules of jurisdiction nor are any reasons provided on why those rules are inadequate or unsatisfactory.

Conclusion

39.15 We consider that reform of the *lex situs* rule for security over moveable property is best considered at an international level in order to promote certainty for parties who

[9] See Chapter 21 above.
[10] See paras 15.33–15.38 above.
[11] See paras 18.18–18.22 above.

commonly deal in different jurisdictions. Moreover, the rule would most appropriately be reviewed within its broader property law application.

39.16 At a UK level, we would welcome any steps to produce a workable rule on how to identify intellectual property as either Scottish or English for the purposes of moveable transactions law and more generally, but this is beyond the scope of this Report.

39.17 Lastly, as in relation to assignation, the general rules on jurisdiction are applicable and we do not recommend reform for cases involving security rights.

Chapter 40 List of recommendations

1. There should be legislative reform of the law of assignation of incorporeal moveable property consisting of the right by a person against another person to the performance of an obligation.

(Paragraph 4.5)

2. The party granting an assignation should be referred to as the "assignor" and the grantee should be referred to as the "assignee".

(Paragraph 4.7; Draft Bill, s 1(2)(a) & (b))

3. The subject matter of the assignation should be referred to as a "claim".

(Paragraph 4.11; Draft Bill, s 1(1))

4. "Claim" should be defined as:

   (a) a right to the performance of an obligation; but

   (b) excluding a non-monetary right relating to land or a negotiable instrument.

(Paragraph 4.16; Draft Bill, s 42(2))

5. The party against whom the claim is enforceable should be referred to as the "debtor".

(Paragraph 4.18; Draft Bill, s 1(2)(c))

6. (a) Agreements to assign claims should not be subject to any requirement of form.

   (b) Assignations of claims should require to be in writing signed by the assignor only. Writing and signature may be electronic as well as paper-and-ink under the rules in the Requirements of Writing (Scotland) Act 1995. The Scottish Ministers should have power to modify the rules as regards execution and authentication in relation to assignations.

(Paragraph 4.24; Draft Bill, ss 1(1), 118(1) & (5))

7. (a) The assignation document should require to identify the claim.

   (b) Where an assignation document assigns multiple claims these should not require to be individually identified provided that they are identified as a class.

(c) For a claim to be transferred it should require to be identifiable as a claim to which the assignation document relates.

(Paragraph 4.30; Draft Bill, ss 1(3) & (4) and 3(1) & (2)(c))

8. (a) It should be competent to assign a claim in whole or in part.

(b) But if the claim is not a monetary claim, the claim should only be assignable in part where either:

(i) the debtor consents, or

(ii) the claim –

(a) is divisible, and

(b) assigning it in part does not result in its becoming significantly more burdensome for the debtor.

(c) But these rules should be subject to

(i) any agreement of the parties to the claim or,

(ii) where the claim arises from a unilateral undertaking, any statement by the person giving the undertaking,

in relation to the extent to which the claim is assignable.

(d) Except in so far as the debtor and the assignor otherwise agree, the assignor should be liable to the debtor for any expense incurred by the debtor because the claim was assigned in part rather than in whole.

(Paragraph 4.34; Draft Bill, s 6)

9. A claim should be transferred on:

(a) the assignation being intimated to the debtor, or

(b) the assignation being registered in the Register of Assignations,

but the Scottish Ministers should have the power to specify categories of claim where registration is required for transfer.

(Paragraph 5.22; Draft Bill, s 3(1), (2)(b) & (6))

10. “Intimate/intimation” should not be replaced by “notify/notification”.

(Paragraph 5.24)

11. Intimation of the assignation of a claim should be effected and only effected:

(a) by there being served on the debtor written notice of the assignation,

(b) by the debtor acknowledging to the assignee that a claim is assigned, or

(c) by it being intimated to the debtor, in judicial proceedings to which the debtor is a party, that the assignation is founded on in the proceedings.

12. The Transmission of Moveable Property (Scotland) Act 1862 should be repealed.

(Paragraph 5.37; Draft Bill, ss 9(1) and 41)

13. Where intimation is by means of written notice to the debtor, it should be possible for the notice to be served by or on behalf of either the assignor or assignee.

(Paragraph 5.40; Draft Bill, ss 9(1)(a) and 118(4))

14. A notice of an assignation:

(a) should

(i) set out the name and address both of the assignor and assignee, and

(ii) provide details of the claim assigned (or, in the case of a claim assigned in part, both of the claim and of the part assigned),

but where the notice is transmitted electronically it can provide an electronic link to a website or portal containing this information.

(b) should not require to be executed or authenticated,

(c) if the claim is a monetary claim, may but need not be in a form prescribed by the Scottish Ministers, and

(d) may consist of, or be contained within:

(i) a single document, or

(ii) more than one document,

and "document" should be defined to include an e-mail or an attachment to an e-mail.

(Paragraph 5.47; Draft Bill, s 9(3) & (5))

15. (a) A notice of an assignation should require to be served:

(i) by being delivered personally to the debtor,

(ii) by being sent by post or by courier either to the proper address of the debtor or to an address for postal communication provided to the assignor by the debtor,

(iii) by being transmitted to an electronic address provided to the assignor by the debtor.

(b) The proper address of the debtor should be:

(i) in the case of a body corporate, the address of the registered or principal office of the body,

(ii) in the case of a partnership, the address of the principal office of the partnership, and

(iii) in any other case, the last known address of the debtor.

(c) Where a notice is posted to an address in the United Kingdom, it should be taken to have been received 48 hours after it is sent unless it is shown to have been received earlier.

(d) Where a notice is sent electronically, it should be taken to have been received 24 hours after it is sent unless it is shown to have been received earlier.

(e) The debtor and the holder of the claim (or the person whose unilateral undertaking gives rise to the claim) should be able in writing to determine that:

(i) only certain of the above methods of service are to apply as respects the claim, or

(ii) postal service is to be to a specified address of the debtor.

(f) It should be competent for intimation to be made or received by authorised representatives of the parties.

(Paragraph 5.57; Draft Bill, ss 9(4) & (6) to (13) and 118(4))

16. Any rule of law whereby an assignation is rendered ineffective by an instruction by the assignee to the debtor to perform to the assignor should be abolished.

(Paragraph 5.61; Draft Bill, s 17(1)(b))

17. Where there are co-debtors, intimation to any one or more of them should be treated as intimation to all of them.

(Paragraph 5.66; Draft Bill, s 9(2))

18. Priority of assignations should continue to be determined by time of completion of title.

(Paragraph 5.72)

19. (a) It should be competent to make the assignation of a claim subject to a condition which must be satisfied before the claim is transferred. Such a condition could depend on something happening or not happening (whether or not it is certain that that thing will or will not happen) or on a period of time elapsing during which something must not happen (whether it is certain or not that the thing will happen at some time.)

(b) Any such condition should require to be specified in the assignation document.

(c) It should be permissible for the specification to include reference to another document the terms of which are not reproduced in the assignation document.

(d) The claim should not transfer until the condition is satisfied.

(Paragraph 5.80; Draft Bill, ss 2 and 3(1) & (2)(d))

20. It should be competent to assign a claim which does not exist at the time that the assignation document is granted, but for the claim to be transferred it should require to have come into being and be held by the assignor.

(Paragraph 5.97; Draft Bill, ss 1(5) and 3(2)(a))

21. In relation to the transfer of claims which arise after the assignation document is granted, any rule of law as to accretion should be disregarded.

(Paragraph 5.100; Draft Bill, s 3(3))

22. (a) Individuals should be prohibited from assigning a claim in respect of wages or salary, including any fee, bonus, commission, holiday pay or other emolument referable to their employment, or to expenses or a redundancy payment.

(b) This rule should be without prejudice to any other enactment.

(Paragraph 5.103; Draft Bill, s 8)

23. (a) An assignation granted before the assignor becomes insolvent should be ineffective as regards a claim if the assignor is insolvent at the time of becoming the holder of the claim.

(b) An assignor who is an individual, or the estate of which may be sequestrated, becomes insolvent when:

(i) the assignor's estate is sequestrated,

(ii) the assignor grants a trust deed for creditors or makes a composition or arrangement with creditors,

(iii) a voluntary arrangement proposed by the assignor is approved, or

(iv) the assignor's application for a debt payment programme is approved under section 2 of the Debt Arrangement and Attachment (Scotland) Act 2002.

(c) An assignor which is not an individual becomes insolvent when:

(i) a decision approving a voluntary arrangement entered into by the assignor has effect under section 4A of the Insolvency Act 1986,

(ii) the assignor is wound up under Part 4 or 5 of the 1986 Act or under section 367 of the Financial Services and Markets Act 2000,

(iii) an administrative receiver, as defined in section 251 of the 1986 Act, is appointed over all or part (being a part which includes the claim) of the property of the assignor, or

(iv) the assignor enters administration, ("enters administration" being construed in accordance with paragraph 1(1) and (2) of schedule B1 of the 1986 Act).

(d) The above rule should not apply as regards a claim in respect of income from property but only in so far as the claim:

(i) is not attributable to anything agreed to by, or done by, the assignor after the assignor becomes insolvent, and

(ii) relates to the use of property in existence at the time the assignor became insolvent.

(e) The Scottish Ministers should have power to amend the definition of "insolvent".

(Paragraph 5.109; Draft Bill, s 5(1) to (4), (7)(a) & (8))

24. (a) Where a person who has assigned a claim in whole or in part is discharged following either sequestration or the granting of a protected trust deed the assignation should be ineffective as regards the claim (or part) to which it relates if, as at the time of discharge, the claim has not come into being.

(b) The Scottish Ministers should have the power to amend the above rule to apply it to other insolvency processes.

(Paragraph 5.112; Draft Bill, s 5(5), (6) & (7)(b))

25. A new public register should be established, to be called the Register of Assignations, in which assignations of claims can be registered.

(Paragraph 6.7; Draft Bill, s 19(1))

26. The register should be under the management and control of the Keeper of the Registers of Scotland.

(Paragraph 6.10; Draft Bill, s 19(2))

27. The assignation document should be registered.

(Paragraph 6.30; Draft Bill, s 21(1)(h))

28. (a) Subject to the requirements of statute, the register should be in such form as the Keeper thinks fit.

(b) The Keeper should take such steps as appear reasonable to her for protecting the register from interference, unauthorised access, or damage.

(Paragraph 6.32; Draft Bill, s 19(3) & (4))

29. Registration should be by electronic means only.

(Paragraph 6.39)

30. Registration should be by means of an automated system under which applications are not checked by the Keeper.

(Paragraph 6.45; Draft Bill, s 119)

31. The Keeper should make up and maintain, as parts of the Register of Assignations:

(a) the assignations record and

(b) the archive record.

(Paragraph 7.2; Draft Bill, s 20)

32. An entry in the assignations record should include:

(a) the assignor's name and address,

(b) where the assignor is an individual, the assignor's date of birth,

(c) any number which the assignor bears or other information relating to the assignor which, by virtue of RoA Rules, must be included in the entry,

(d) the assignee's name and address,

(e) any number which the assignee bears or other information relating to the assignee which, by virtue of RoA Rules, must be included in the entry,

(f) where the assignee is not an individual, an address (which may be an e-mail address) to which requests for information regarding the assignation may be directed,

(g) such description of the claim as may be required or permitted by RoA Rules,

(h) a copy of the assignation document,

(i) the registration number allocated to the entry,

(j) the date and time of registration of the assignation document, and

(k) such other data as may be required by legislation.

(Paragraph 7.27; Draft Bill, s 21(1))

33. (a) An application for registration of an assignation document should be made by or on behalf of the assignee.

(b) The Keeper should be required to accept an application if:

(i) it conforms to RoA Rules in relation to applications,

(ii) it is submitted with a copy of the assignation document,

(iii) it provides the Keeper with the necessary data to make up an entry for the assignation in the RoA, and

(iv) the registration fee is paid or the Keeper is satisfied that it will be.

(c) Where these requirements are not satisfied, the Keeper should be required to reject the application and inform the applicant accordingly.

(Paragraph 7.30; Draft Bill, s 23(1) to (3) and 118(4))

34. On accepting an application for registration, the Keeper should be required to:

(a) make up and maintain in the assignations record an entry for the assignation document, and

(b) allocate a registration number to the entry.

(Paragraph 7.32; Draft Bill, s 23(4))

35. (a) The Keeper should be required to issue a verification statement on accepting an application for registration.

(b) The statement should require to conform to RoA Rules. It should include the date and time of the registration and the registration number allocated to the entry to which the application relates.

(c) The assignor should be entitled to obtain a copy of the verification statement from the assignee and the assignee should be required to supply the copy within 21 days after the request is made.

(Paragraph 7.40; Draft Bill, s 24)

36. (a) A registration should be taken to be made on the date and at the time which are entered for it in the Register of Assignations.

(b) The Keeper should be required to deal with applications for registration and allocate these registration numbers in order of receipt.

(Paragraph 7.42; Draft Bill, s 25)

37. The registration of an assignation document should be ineffective if:

(a) the entry made up for it does not include a copy of the assignation document,

(b) that document is invalid, or

(c) there is an inaccuracy in relation to the data registered, which as at the time of registration, is seriously misleading.

(Paragraph 8.15; Draft Bill, s 26(1))

38. (a) An inaccuracy in an entry in the assignations record may be seriously misleading irrespective of whether any person has been misled.

(b) In determining whether an inaccuracy is seriously misleading no account should be taken of the assignation document included in the entry.

(c) An inaccuracy which is seriously misleading in respect of part of an entry, as regards the details of the claim, assignor or assignee, should not affect the rest of the entry.

(d) Without prejudice to the generality, an inaccuracy should be seriously misleading:

(i) where the assignor (or, as the case may be, a co-assignor) is not a person required by RoA Rules to be identified by a unique number, if a search using a designated facility provided by the Keeper for

(a) the assignor's (or co-assignor's) proper name as at the date and time the entry was created, or for

(b) the assignor's (or co-assignor's) proper name as at that date and time and the assignor's (or co-assignor's) date of birth

does not disclose the entry;

(ii) where the assignor (or, as the case may be, a co-assignor) is a person required by RoA Rules to be identified by a unique number, if a search using a designated facility provided by the Keeper for that number as at the date and time the entry was created does not disclose the entry, including where a search using such a facility for the assignor's (or co-assignor's) number does disclose the entry.

(e) The meaning of "proper name" should be set out in RoA Rules.

(f) The Scottish Ministers should have the power to specify further instances in which an inaccuracy is seriously misleading.

(Paragraph 8.30; Draft Bill, s 27)

39. Except in so far as the context otherwise requires, any reference to "correction" should include correction by:

(a) the removal of data included in an entry,

(b) the removal of an entry from the assignations record and the transfer of that entry to the archive record,

(c) the replacement of data, or of a copy document, included in an entry,

(d) the restoration of data, or of a copy document, to an entry,

(e) the restoration of an entry (whether or not by removing it from the archive record and transferring it to the assignations record).

(Paragraph 9.9; Draft Bill, s 31(1))

40. (a) Where the Keeper becomes aware of a manifest inaccuracy in an entry in the assignations record the Keeper should have to correct the inaccuracy if what is needed to correct it is manifest. If what is needed to correct is not manifest the Keeper should have to note the inaccuracy on the entry.

(b) Where an inaccuracy is corrected by:

(i) removal of the entry the Keeper should have to transfer the entry to the archive record and note on the entry the details of the correction, and its date and time,

(ii) removal or replacement of data included in the entry or by replacement of a copy document the Keeper should have to note on the entry the details of the correction, and its date and time,

(iii) replacement of a copy document, the Keeper should have to transfer it to the archive record.

(c) Where the Keeper effects a correction, the Keeper should have to notify each person specified for these purposes by RoA Rules and any other person whom the Keeper considers it appropriate to notify that the correction has been effected.

(Paragraph 9.22; Draft Bill, s 28)

41. (a) Where a court determines that the assignations record is inaccurate it should have the power to direct the Keeper to correct it.

(b) In connection with any such correction, the court should be able to give the Keeper such further direction (if any) as it considers requisite.

(c) The Keeper should be required to note on the relevant entry that it has been corrected and the details of the correction, including the date and time. Where the correction requires the removal of the entry or of a copy document the Keeper should have to transfer it to the archive record.

(d) Where the Keeper effects a correction, the Keeper should have to notify each person specified for these purposes by RoA Rules and any other person whom the Keeper considers it appropriate to notify that the correction has been effected.

(Paragraph 9.27; Draft Bill, s 29)

42. The Keeper should be entitled to appear and be heard in any civil proceedings, whether before a court or tribunal, in which is put in question (either or both):

(a) the accuracy of the assignations record,

(b) what is needed to correct an inaccuracy in that record.

(Paragraph 9.29; Draft Bill, s 30)

43. A registration which is ineffective should become effective if and when the entry is corrected.

(Paragraph 9.32; Draft Bill, s 26(3))

44. A correction should be taken to be made on the date and at the time which are entered for it in the register.

(Paragraph 9.34; Draft Bill, s 31(2))

45. The assignations record should be searchable only:

(a) by reference to any of the following data in the entries contained in that record:

(i) the names of assignors,

(ii) the names and dates of birth of assignors who are individuals,

(iii) the unique numbers of assignors required by RoA Rules to be identified in the assignations record by such a number,

(b) by reference to registration numbers allocated to entries in that record, or

(c) by reference to some other factor, or characteristic, specified for these purposes by RoA Rules.

(Paragraph 10.10; Draft Bill, s 32(2))

46. A person should be able to search the assignations record if the search accords with RoA Rules and either the appropriate fee is paid or the Keeper is satisfied that it will be paid.

(Paragraph 10.17; Draft Bill, s 32(1))

47. (a) The Keeper should be required to provide a search facility in relation to which the search criteria are specified by RoA Rules, but may provide such other search facilities, with such other search criteria, as the Keeper thinks fit.

(b) "Search criteria" should be defined as the criteria in accordance with which what is searched for must match data in an entry in order to retrieve the entry.

(Paragraph 10.29; Draft Bill, s 33)

48. A printed search result which purports to show an entry in the assignations record should be admissible in evidence, and in the absence of evidence to the contrary, should be sufficient proof of:

(i) the registration of the assignation document to which the result relates,

(ii) a correction of the entry in the assignations record to which the result relates, and

(iii) the date and time of such registration or correction.

(Paragraph 10.31; Draft Bill, s 34)

49. (a) Any person should be able to apply to the Keeper for an extract of an entry in the register.

(b) The Keeper should be required to issue the extract if the appropriate fee is paid or the Keeper is satisfied that it will be paid.

(c) The Keeper should be able to validate the extract as the Keeper considers appropriate.

(d) The Keeper should be able to issue the extract as an electronic document if the applicant does not require that it be issued as a traditional document.

(e) The extract should be accepted for all purposes as sufficient evidence of the contents, as at the date on which and the time at which the extract is issued (being a date and time specified in the extract), of the entry.

(Paragraph 10.34; Draft Bill, s 35)

50. (a) An entitled person should be entitled to request from the person identified in an entry in the assignations record as the assignee a written statement as to:

(i) whether or not a claim specified in the notice is assigned; or

(ii) whether a condition to which the assignation is subject has been satisfied.

(b) The following should be entitled persons:

(i) a person who has the right to execute diligence against a claim specified in the notice (or who is authorised by decree to execute a charge for payment and will have the right to execute diligence against that claim if and when the days of charge expire without payment) depending on whether the claim has been assigned by the assignation,

(ii) a person who is prescribed for these purposes, and

(iii) a person who has the consent of the person identified in the entry as the assignor.

(Paragraph 11.10; Draft Bill, s 36(1) to (3))

51. (a) An information request should require to be complied with within 21 days of its receipt, unless:

(i) a court is satisfied that in all the circumstances this would be unreasonable and either extends the 21-day period or exempts the recipient from complying with the request in whole or in part,

(ii) it is manifest from the entry that the claim specified in the notice has not been assigned by the assignation document or that the registration is ineffective, or

(iii) the same request has been made by the same person within the last 3 months and the information supplied in response to the last request has not changed.

(b) The recipient should be entitled to recover from the requester any costs reasonably incurred in complying with the request.

(c) If a court is satisfied on the application of the requester that the recipient has not complied with the duty to provide information without reasonable excuse it should by order require that the recipient complies within 14 days.

(Paragraph 11.17; Draft Bill, s 36(4) to (8))

52. The archive record should be the totality of all the entries transferred from the assignations record following a correction and include other data specified by RoA Rules.

(Paragraph 11.21; Draft Bill, s 22)

53. (a) A person should be entitled to be compensated by the Keeper for loss suffered in consequence of:

(i) an inaccuracy attributable to the Keeper in the making up, maintenance or operation of the Register of Assignations, or in an attempted correction of the register,

(ii) the issue of a statement or notification which is incorrect, or

(iii) the issue of an extract which is not a true extract.

(b) But the Keeper should have no statutory liability:

(i) in so far as the person's loss could have been avoided had the person taken measures which it would have been reasonable for the person to take,

(ii) in so far as the person's loss is not reasonably foreseeable, or

(iii) for non-patrimonial loss.

(Paragraph 11.34; Draft Bill, s 37)

54. (a) Where a person suffers loss in consequence of:

(i) an inaccuracy in an entry in the Register of Assignations (which is not caused by the Keeper), the person should be entitled to be compensated for that loss by the person who made the application which gave rise to that entry if, in making it, that person failed to take reasonable care, or

(ii) a failure to respond to a request for information under the information duty provisions, or the provision of information in which there is an inaccuracy, the person is entitled to be compensated for that loss by the person who failed to supply the information if that failure was without reasonable cause or if, in supplying it, that person failed to take reasonable care.

(b) But there should be no liability:

(i) in so far as the person's loss could have been avoided had the person taken measures which it would have been reasonable for the person to take,

(ii) in so far as the loss is not reasonably foreseeable, or

(iii) for non-patrimonial loss.

(Paragraph 11.42; Draft Bill, s 38)

55. The Scottish Ministers should, following consultation with the Keeper, have the power to make rules (to be known as "RoA Rules"):

(a) as to the making up and keeping of the register,

(b) as to procedure in relation to applications:

(i) for registration, or

(ii) for corrections,

(c) as to the identification, in any such application of any person or claim, including:

(i) how the proper form of a person's name is to be determined, and

(ii) where the person bears a number (whether of numerals or of letters and numerals) unique to the person, whether that number must (or may) be used in identifying the person,

(d) as to the degree of precision with which time is to be recorded in the register,

(e) as to the manner in which an inaccuracy in the assignations record may be brought to the attention of the Keeper,

(f) as to information which, though contained in an assignation document, need not be included in a copy of that document submitted with an application for registration,

(g) as to whether a signature contained in an assignation document need be included in a copy of that document so submitted,

(h) as to searches in the register,

(i) as to information which, though contained in the register, is not to be:

(i) available to persons searching it, or

(ii) included in any extract issued by the Keeper,

(j) prescribing the configuration, formatting and content of:

(i) applications,

(ii) notices,

(iii) documents,

(iv) data,

(v) statements, and

(vi) requests,

to be used in relation to the register,

(k) as to when the register is open for:

(i) registration, and

(ii) searches,

(l) requiring there to be entered in the assignations record or the archive record such information as may be specified in the rules, or

(m) regarding other matters in relation to registration, being matters for which the Scottish Ministers consider it necessary or expedient to give full effect to the purposes of the draft Bill.

(Paragraph 11.49; Draft Bill, s 40)

56. (a) Where after a claim has been transferred by assignation there is performance by the debtor or any co-debtor to the assignor and that performance is in good faith, the debtor should be discharged to the extent of the performance.

(b) The fact only that an assignation document has been registered or that a notice of an assignation has been deemed to have been received, should not of itself mean that a debtor, or any co-debtor, is to be regarded as having performed other than in good faith.

(c) In any dispute as to whether performance was in good faith the burden of proof should lie on the party asserting that performance was other than in good faith.

(Paragraph 12.9; Draft Bill, ss 11 and 120)

57. (a) Where a claim (or one and the same part of a claim) has been assigned successively, the debtor should be discharged to the extent that the debtor (or any co-debtor) performs in good faith to the first assignee from whom intimation is received.

(b) The fact only that an assignation document has been registered or that a notice of an assignation has been deemed to have been received, should not of itself mean that a debtor, or any co-debtor, is to be regarded as having performed other than in good faith.

(c) In any dispute as to whether performance was in good faith the burden of proof should lie on the party asserting that performance was other than in good faith.

(Paragraph 12.12; Draft Bill, ss 12 and 120)

58. (a) Where a claim is of a type that has been prescribed as transferable only by registration and an assignation of that claim is not registered, but intimation of it is made to the debtor or a co-debtor, the debtor should be discharged to the extent that performance is made in good faith to the assignee.

(b) A debtor or co-debtor who knows that the assignation has not been registered and that transfer of the claim requires such registration should not be taken to perform in good faith.

(Paragraph 12.15; Draft Bill, s 13)

59. (a) A debtor to whom intimation of an assignation has been made by an assignee should be entitled to request from the assignee sufficient evidence of the assignation.

(b) "Sufficient evidence" should include the written confirmation of an assignor that an assignation to which that assignor is party has taken place.

(c) A debtor who has reasonable grounds to believe that a claim has been assigned should be entitled to ask the supposed assignor whether there has been an assignation.

(d) The supposed assignor should have to confirm in writing whether the claim has been assigned.

(e) Until the debtor receives the evidence or confirmation, the debtor should be entitled to withhold performance.

(Paragraph 12.26; Draft Bill, s 15)

60. (a) The *assignatus utitur jure auctoris* rule should be put into statutory form, that is to say the debtor (or any co-debtor) should be able to assert against the assignee all defences that the debtor could assert against the assignor.

(b) The debtor (or any co-debtor) should be able to assert against the assignee any right of compensation (including a right of contractual set-off where the basis of that right is the contract which gave rise to the claim) available to the debtor against the assignor up to the time when the debtor would no longer have been in good faith had the debtor performed to the assignor.

(c) The fact only that an assignation document has been registered or that a notice of an assignation has been deemed to have been received, should not of itself mean that a debtor, or any co-debtor, is to be regarded as having performed other than in good faith.

(Paragraph 12.34; Draft Bill, s 14(1) to (3) & (5))

61. (a) The debtor and the assignor should be able to agree that any defences which the debtor may assert against the assignor may not be asserted against an assignee.

(b) This should be without prejudice to any other enactment.

(Paragraph 12.38; Draft Bill, s 14(1) & (4))

62. (a) The ability of the holder of a claim to assign should be subject to any enactment, or any rule of law, by virtue of which a claim is not assignable.

(b) Subject to any other enactment, an assignation of a claim should be ineffective in so far as the debtor and the holder of the claim agree, or the person whose unilateral undertaking gives rise to the claim states, that the claim is not to be assigned.

(Paragraph 13.11; Draft Bill, s 7)

63. (a) The following rules of law should no longer have effect:

(i) any rule whereby a mandate may operate as an assignation of a claim;

(ii) any rule whereby an assignee of a claim may sue in the name of an assignor.

(b) But this should be without prejudice to the application of any enactment or rule of law as respects subrogation.

(Paragraph 13.20; Draft Bill, s 17(1)(a) & (c), and (2))

64. The Policies of Assurance Act 1867 should be amended to confirm that it does not apply in Scotland.

(Paragraph 13.23)

65. There should be no statutory provision made in relation to the transfer of entire contracts.

(Paragraph 13.25)

66. (a) Unless the assignor and assignee provide otherwise in the assignation document, where a claim is assigned in whole, the assignee should acquire, by virtue of the assignation, any security which relates to the claim assigned and is restricted to that claim.

(b) The assignee should be required to perform any act requisite for the transfer of the security to the assignee as soon as reasonably practicable.

(Paragraph 13.33; Draft Bill, s 16)

67. (a) In assigning a claim for value the assignor should be taken to warrant to the assignee that:

(i) the assignor is entitled to, or (in the case of a future claim) will be entitled to, transfer the claim to the assignee,

(ii) the debtor is obliged to perform in full to the assignor, and

(iii) the assignor has done nothing and will do nothing to prejudice the assignation.

(b) In assigning a claim other than for value the assignor should be taken to warrant to the assignee that the assignor will do nothing to prejudice the assignation.

(c) In assigning a claim, whether for value or other than for value, the assignor should not be taken to warrant to the assignee that the debtor will perform to the assignee.

(d) These rules should also apply to any contract or unilateral undertaking which the assignation implements.

(e) These rules should be subject to contrary agreement by the parties.

(f) The common law rules on warrandice in relation to the assignation of claims should be abolished.

(Paragraph 13.43; Draft Bill, ss 10 and 17(1)(d))

68. The general provisions on assignation of claims should be without prejudice to the application, as respects the assignment and acquisition of associated rights, of the International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015.

(Paragraph 13.46; Draft Bill, s 18)

69. At the present time the law of assignation of claims should not be codified.

(Paragraph 13.49)

70. (a) If an assignation document evidences a security financial collateral arrangement or a title transfer financial collateral arrangement (as defined in regulation 3 of the Financial Collateral Arrangements (No. 2) Regulations 2003) in respect of a claim, then the transfer of that claim should require either (i) intimation to the debtor or registration in the Register of Assignations, or (ii) the financial collateral

in question to come into the possession of, or under the control of, the collateral-taker or a person authorised to act on the collateral-taker's behalf.

(b) In case (ii) the assignation document need not be executed or signed electronically and may be created as writing transcribed by electronic or other means in a durable medium, or as sounds recorded in such a medium.

(Paragraph 14.43; Draft Bill, s 4)

71. The law on security over moveable property should be reformed on the lines set out in Chapter 16.

(Paragraph 18.74)

72. (a) There should be a new right in security over moveable property.

(b) It should be a new type of pledge called a "statutory pledge".

(Paragraph 19.8; Draft Bill, s 43(1), (2)(b) & (4))

73. (a) The person to whom a pledge is granted should be referred to as the "secured creditor".

(b) The person who grants the pledge should be referred to as the "provider".

(Paragraph 19.12; Draft Bill, s 43(5))

74. (a) The term "provider" should include any successor in title or representative of a provider (unless the successor or representative is a person who acquired the encumbered property unencumbered by the statutory pledge in question).

(b) The term "secured creditor" should include any successor in title or representative of a secured creditor.

(Paragraph 19.15; Draft Bill, s 116(1))

75. The secured obligation:

(a) may be any obligation owed, or which will or may become owed, to the secured creditor,

(b) should not require to be an obligation owed

(i) by the provider, or

(ii) to the secured creditor, and

(c) should include ancillary obligations owed to the secured creditor (as for example to pay interest, damages or the reasonable expenses of extra-judicial recovery of interest or damages).

(Paragraph 19.26; Draft Bill, s 44(2))

76. There should not be a non-accessory form of pledge.

(Paragraph 19.30)

77. Any person, juristic or natural, should be able to grant a pledge.

(Paragraph 19.35)

78. (a) Where the provider of a statutory pledge is an individual the encumbered property should require to consist only of assets separately identified in the constitutive document (or in any amendment document) and which are either:

(i) the provider's property at the time that document is granted, or

(ii) acquired by the provider after that time if the acquisition is financed by credit and an obligation to repay that credit is the secured obligation.

(b) A corporeal asset so identified should require, immediately before that document is granted, to have a monetary value exceeding £1,000 or such other prescribed amount.

(Paragraph 19.51; Draft Bill, s 52(1) to (3))

79. The restrictions on the grant of a statutory pledge in relation to individuals should not apply to sole traders as respects any assets used, or to be used, wholly or mainly for the purposes of that sole trader's business.

(Paragraph 19.55; Draft Bill, s 52(4))

80. It should be competent to grant a statutory pledge over moveable property but not over property that has acceded to immoveable (heritable) property.

(Paragraph 19.60; Draft Bill, s 43(1))

81. The encumbered property should require to be transferable (whether or not its transferability is restricted in some way).

(Paragraph 19.64; Draft Bill, s 44(4))

82. The encumbered property should (except in so far as the provider and the secured creditor agree otherwise) include the natural fruits, but not the incorporeal fruits, of the property.

(Paragraph 19.71; Draft Bill, s 44(3)(b))

83. There should not be a special regime for construction contracts.

(Paragraph 19.72)

84. (a) The statutory pledge should be a fixed security only.

(b) The definitions of "fixed security" in the Companies Act 1985 and the Insolvency Act 1986 should be amended to include reference to the statutory pledge.

(Paragraph 20.26; Draft Bill, s 65)

85. The secured creditor should not be able to give the provider a general mandate to deal with the encumbered property free of the statutory pledge.

(Paragraph 20.36)

86. (a) If the provider of a statutory pledge transfers encumbered property to a third party other than with the consent mentioned below, the property should remain subject to the pledge.

(b) That consent should be the written consent of the secured creditor to the particular transfer and to the property in question being transferred unencumbered by the pledge, but should not include consent granted more than 14 days before the particular transfer.

(c) The granting or withholding of consent should require to be at the discretion of the secured creditor.

(d) The Scottish Ministers should have the power to make regulations amending the rules relating to consent.

(e) The foregoing recommendations should be subject to the recommendations made elsewhere as regards good faith acquirers.

(Paragraph 20.45; Draft Bill, s 53(1) to (3), (5) & (6))

87. A statutory pledge should be extinguished if the secured creditor acquiesces, expressly or impliedly, in the provider's transfer of the encumbered property or any part of it to a third party other than with the consent required by the legislation.

(Paragraph 20.53; Draft Bill, s 53(4))

88. It should be competent to create a statutory pledge over corporeal moveable property.

(Paragraph 21.3; Draft Bill, s 43(1), (2)(b) and (4))

89. For the purposes of the new legislative scheme in relation to pledge, the definition of "corporeal moveable property" should not include money.

(Paragraph 21.6; Draft Bill, s 116(1))

90. It should not be competent to create a statutory pledge over a ship (or a share of a ship) in respect of which it is competent to register a mortgage in the UK Ship Register.

(Paragraph 21.10; Draft Bill, s 47(1)(c))

91. It should not be competent to create a statutory pledge over an aircraft in respect of which an aircraft mortgage can be created.

(Paragraph 21.12; Draft Bill, s 47(1)(a))

92. The prescribed style for Scottish aircraft mortgages should be deleted from the Mortgaging of Aircraft Order 1972.

(Paragraph 21.14)

93. The Mortgaging of Aircraft Order 1972 should be the subject of a UK-wide review.

(Paragraph 21.15)

94. It should not be competent to create a statutory pledge over an aircraft object in respect of which an international security interest can be created under the International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015.

(Paragraph 21.20; Draft Bill, s 47(1)(b))

95. It should be possible to create a statutory pledge over financial instruments within the meaning of regulation 3(1) of the Financial Collateral Arrangements (No. 2) Regulations 2003.

(Paragraph 22.34; Draft Bill, ss 47(2)(c) and 116(1))

96. It should be possible to create a statutory pledge over:

(a) intellectual property, and

(b) applications for, or licences over, intellectual property.

(Paragraph 22.43; Draft Bill, s 47(2)(a) and (b))

97. In the case of registered intellectual property, registration of the statutory pledge in the relevant intellectual property register should not displace the requirement for registration in the Register of Statutory Pledges, but consideration should be given to establishing information-sharing arrangements between the registers.

(Paragraph 22.54)

98. Any rule of law in relation to a pledge over a negotiable instrument should be unaffected by the reforms recommended in this Report.

(Paragraph 22.60; Draft Bill, s 43(6))

99. The Scottish Ministers should have the power to prescribe other kinds of incorporeal moveable property over which a statutory pledge may be created.

(Paragraph 22.62; Draft Bill s 47(2)(d))

100. (a) A statutory pledge should require a constitutive document.

(b) The constitutive document should require to:

(i) be executed or authenticated by the provider,

(ii) identify the property which is to be encumbered property (which may be either property of, or property to be acquired by, the provider), and

(iii) identify the secured obligation.

(c) If the encumbered property is to consist of more than one item the constitutive document should not have to identify each item separately provided that the document identifies the items in terms of their constituting an identifiable class.

(Paragraph 23.10; Draft Bill, s 46)

101. Registration in the Register of Statutory Pledges should be a pre-requisite for the creation of a statutory pledge.

(Paragraph 23.19; Draft Bill, ss 48 to 49)

102. (a) A statutory pledge over property which, at the time the statutory pledge is registered, is the provider's and is identifiable as property to which the constitutive document relates, is created over that property on registration.

(b) If the property is not yet so identifiable, the statutory pledge is created over that property on it becoming so identifiable.

(Paragraph 23.21; Draft Bill, s 48(1) & (2))

103. A statutory pledge should be created over after-acquired property when the property becomes the provider's property, provided that the property is identifiable at that time as property which is to be encumbered property. If it is not so identifiable at that time then the pledge should not be created until such time as it does become so identifiable.

(Paragraph 23.27; Draft Bill, s 51)

104. (a) A statutory pledge granted prior to the provider becoming insolvent should not be able to encumber property acquired after that time.

(b) A provider who is an individual, or the estate of which may be sequestrated, becomes insolvent when:

(i) the provider's estate is sequestrated,

(ii) the provider grants a trust deed for creditors or makes a composition or arrangement with creditors,

(iii) a voluntary arrangement proposed by the provider is approved,or

(iv) the provider's application for a debt payment programme is approved under section 2 of the Debt Arrangement and Attachment (Scotland) Act 2002.

(c) A provider which is not an individual becomes insolvent when:

(i) a decision approving a voluntary arrangement entered into by the provider has effect under section 4A of the Insolvency Act 1986,

(ii) the provider is wound up under Part 4 or 5 of the 1986 Act or under section 367 of the Financial Services and Markets Act 2000,

(iii) an administrative receiver is appointed over all or part of the property of the provider including the encumbered property, or

(iv) the assignor enters administration, ("enters administration" being construed in accordance with paragraph 1(1) and (2) of schedule B1 of the 1986 Act).

(d) The Scottish Ministers should have power to amend the definition of "insolvent".

(Paragraph 23.32; Draft Bill, s 51)

105. (a) The secured creditor and the provider should be entitled to amend a statutory pledge by means of an executed or authenticated amendment document.

(b) An amendment document which relates to the addition of property to the encumbered property must identify the property to be added. That property may either be property of, or property to be acquired by the provider.

(c) An amendment document by virtue of which only an amendment adding property to the encumbered property is made need not be executed or authenticated by the secured creditor.

(d) Where an amendment document relates to (either or both):

(i) the addition of property to the encumbered property,

(ii) variation of the secured obligation, where the extent of that obligation is to be increased and its current extent is determinable from the entry alone,

the statutory pledge should be amended only on registration of that document.

(e) On the amendment being registered in respect of additional property, the statutory pledge is created over that property provided that it:

(i) is identifiable as property which is to be encumbered property, and

(ii) is the property of the provider.

(Paragraph 23.40; Draft Bill, ss 49 and 60)

106. (a) Except in so far as the provider and the secured creditor otherwise agree, a statutory pledge should be transferable by means of an assignation document executed or authenticated by the secured creditor.

(b) Subject to the provisions of the assignation document, the assignation should convey to the assignee entitlement to the benefit of any noticed served, or enforcement procedure commenced, by the assignor in respect of the statutory pledge before assignation.

(Paragraph 23.48; Draft Bill, s 59(1) to (2))

107. It should be possible to restrict a statutory pledge to part of the encumbered property or to discharge it by means of a written statement made by the secured creditor.

(Paragraph 23.54; Draft Bill, s 61(1))

108. (a) A person who purchases corporeal property which is encumbered property and which is, or has been transferred without the required consent of the secured creditor, should acquire it unencumbered by the statutory pledge if:

(i) the person from whom the property is acquired is acting in the ordinary course of that person's business, and

(ii) at the time of acquisition, the person is in good faith.

(b) A person should not be taken to be other than in good faith by reason only of the pledge having been registered.

(Paragraph 24.24; Draft Bill, s 54)

109. (a) An individual who acquires corporeal property which is encumbered property and which is, or has been, transferred without the required consent of the secured creditor, should acquire it unencumbered by the statutory pledge if:

(i) the value of all that is acquired does not, at the time of acquisition, exceed such amount (if any) as the Scottish Ministers may by regulations specify,

(ii) at the time of acquisition, the acquirer is in good faith,

(iii) the acquirer gives value for the property acquired, and

(iv) the property is wholly or mainly acquired for personal, domestic or household purposes.

(b) This rule should not apply in respect of the acquisition of encumbered property (or any part of that property) which consists of a motor vehicle.

(c) A person should not be taken to be other than in good faith by reason only of the pledge having been registered.

(Paragraph 24.30; Draft Bill, s 55)

110. (a) The following rule should apply where:

(i) there is a sale agreement (or conditional sale agreement) or a hire-purchase agreement in respect of a motor vehicle,

(ii) the motor vehicle is encumbered property,

(iii) the purchaser or hirer is, at the time of entering into the agreement, in good faith, and

(iv) at that time the purchaser or hirer is not a person carrying on a business described in section 29(2) of the Hire-Purchase Act 1964.

(b) On the motor vehicle being transferred to the purchaser or hirer in accordance with the agreement, that person should acquire it unencumbered by the statutory pledge.

(c) And the statutory pledge should not be able to be enforced against the motor vehicle while the agreement is extant, and before the vehicle is transferred to the purchaser or hirer.

(d) But if the transferor is, at the time the agreement is entered into, a person carrying on a business described in section 29(2) of the Hire-Purchase Act 1964, the secured creditor should be entitled to receive from the transferor the lesser of:

(i) the amount outstanding in respect of the secured obligation, and

(ii) the amount received, or to be received, by the transferor in respect of the acquisition.

(e) A purchaser should not be taken to be other than in good faith by reason only of the statutory pledge having been registered.

(f) "Conditional sale agreement", "hire-purchase agreement" and "motor vehicle" should have the meanings given to those expressions by section 29(1) of the Hire-Purchase Act 1964.

(g) The Scottish Ministers should have the power to make regulations specifying the motor vehicles, or classes of motor vehicle, to which these rules are not to apply.

(Paragraph 24.43; Draft Bill, s 56)

111. (a) The following rule should apply where:

(i) a person, in the ordinary course of trading on a specified financial market, acquires a financial instrument of a specified kind, and

(ii) that financial instrument is encumbered property.

(b) The person should acquire the instrument unencumbered by the statutory pledge provided that:

(i) at the time of acquisition the person does not know of the statutory pledge, and

(ii) the acquisition takes place in accordance with the rules of the specified financial market.

(c) "Specified" should mean specified, for these purposes, by the Scottish Ministers by regulations.

(d) The regulations should be able to specify different markets or descriptions of market in relation to different kinds of financial instrument.

(Paragraph 24.48; Draft Bill, s 57)

112. (a) For a possessory pledge to be created the property delivered must be or become the property of the provider.

(b) The rule in *Hamilton v Western Bank*, that pledge is restricted to actual delivery of the property which is to be encumbered, should no longer have effect.

(c) Delivery of corporeal moveable property in order to pledge it should be effected by:

(i) physically handing over or giving control of the property to the secured creditor or to a person authorised to accept delivery on behalf of the secured creditor,

(ii) giving control of the premises in which the property is located to the secured creditor or to a person so authorised,

(iii) instructing an independent third party who has direct possession or custody of the property to hold the property on behalf of the secured creditor or of a person so authorised, or

(iv) delivering a bill of lading to the secured creditor or to a person so authorised (and where that bill is to the order of a particular person, by effecting the endorsement of the bill in favour of the secured creditor).

(d) Property already in the direct possession or custody of the secured creditor or of a person authorised to hold the property on behalf of the secured creditor when agreement on the creation of the pledge is reached between the provider and the secured creditor is deemed to have been delivered to the secured creditor for the purpose of creating a pledge.

(e) These rules should be without prejudice to section 2 of the Factors Act 1889 (powers of mercantile agent with respect to disposition of goods).

(Paragraph 25.10; Draft Bill, ss 45 and 118(4))

113. The rule in *North-Western Bank Limited v Poynter, Son & Macdonalds*, that pledged property can be redelivered to the provider on the basis of a trust receipt without extinguishing the pledge, should not at the present time be abolished.

(Paragraph 25.13)

114. (a) Where, under the pawnbroking provisions of the Consumer Credit Act 1974, ownership of the pledged item is lost because the loan is below the prescribed figure (currently £75), the debt (if more than the value of the item) should be reduced by the value of the item.

(b) Where, under the pawnbroking provisions of the Consumer Credit Act 1974, ownership of the pledged item is lost because the loan is below the prescribed figure (currently £75), but the value of the item exceeds the loan, the loan should be discharged, and the pawnbroker should be obliged to pay the customer the surplus value (subject always to deduction of administrative expenses etc).

(Paragraph 25.17)

115. Possessory pledge should have the same remedies as statutory pledge in non-Consumer Credit Act 1974 cases.

(Paragraph 25.22; Draft Bill, ss 67 to 84)

116. The law of possessory pledge should not be codified at the present time.

(Paragraph 25.24)

117. In general, the priority in ranking of any two pledges, or a pledge and a right in security other than a pledge, should be determined according to their creation, the earlier created having priority over the later.

(Paragraph 26.9; Draft Bill, s 64(1))

118. The priority in ranking of a pledge should be the same irrespective of whether the secured obligation is an obligation owed or is an obligation which will or may become owed.

(Paragraph 26.13; Draft Bill, s 64(5))

119. Where a provider grants two or more statutory pledges over property which, as at the time the pledges are granted, is not the provider's, the priority in ranking of any two of the pledges should be determined according to the dates on which they are registered, the earlier having priority over the later.

(Paragraph 26.19; Draft Bill, s 64(2) & (3))

120. The definitions of "fixed security" in section 486(1) of the Companies Act 1985 and section 70(1) of the Insolvency Act 1986 should be amended to include a statutory pledge.

(Paragraph 26.22; Draft Bill, s 65)

121. Where property is subject both to a pledge and to a security arising by operation of law, the security arising by operation of law should have priority over the pledge.

(Paragraph 26.29; Draft Bill, s 64(4))

122. (a) Where diligence is executed in respect of property all or any part of which is encumbered by a pledge, the pledge has priority of ranking over the diligence, except as regards further advances made after the execution of the diligence which are not required to be made by a contractual agreement entered into or undertaking given before such execution.

(b) Where a pledge is created over property in respect of all or any part of which diligence has been executed, the diligence has priority in ranking over the pledge.

(Paragraph 26.33; Draft Bill, s 66)

123. (a) The secured creditor and the holder of another pledge or other right in security should be able to set out in writing an agreement as to ranking.

(b) Such an agreement should have effect only as between the parties to the agreement and their successors and should not be registrable.

(Paragraph 26.38; Draft Bill, s 64(6) & (7))

124. The statutory pledge should not be enforceable by receivership.

(Paragraph 27.12)

125. In the scheme for the enforcement of pledges, the expression “pledge” should not include a pledge as defined in section 189(1) of the Consumer Credit Act 1974.

(Paragraph 27.17; Draft Bill, s 67)

126. A pledge should be enforceable in no other way than in accordance with the remedies set out in statute.

(Paragraph 27.27; Draft Bill, s 68(1))

127. (a) A statutory pledge should be enforceable:

(i) where there is failure to perform the secured obligation, or

(ii) in such other circumstances, if any, as are agreed between the provider and the secured creditor.

(b) Any such agreement should require to be set out in writing.

(Paragraph 27.28; Draft Bill, s 68(2) & (3))

128. A statutory pledge should be enforceable by or on behalf of the secured creditor.

(Paragraph 27.31; Draft Bill, ss 68 and 118(4))

129. In enforcing a pledge a secured creditor should have a duty to conform with reasonable standards of commercial practice. This duty should be to the provider and third parties with an interest in how the pledge is enforced.

(Paragraph 27.36; Draft Bill, s 68(4))

130. (a) Before taking any steps to enforce a pledge the secured creditor should require to serve a notice on:

(i) the provider,

(ii) the holder of any right in security over all or part of the encumbered property,

(iii) any creditor who has executed diligence against all or part of the encumbered property, and

(iv) any prescribed person who has statutory duties in relation to the provider’s estate.

(b) But the duty in cases (ii) and (iii) is to be waived if the secured creditor does not know and cannot reasonably be expected to know of the right in security or diligence.

(c) Such a notice is to be known as a "Pledge Enforcement Notice" in, or as nearly as may be in, such form as may be prescribed.

(d) The Scottish Ministers should have the power to prescribe different forms for different categories of provider.

(e) If by virtue of the Consumer Credit Act 1974, a default notice must be served on the provider, the requirements of that Act in relation to such a notice should require to be satisfied before a Pledge Enforcement Notice can be served.

(Paragraph 27.45; Draft Bill, s 69)

131. (a) A court order should not generally be required to enforce a pledge.

(b) Such an order should be required where the provider of a pledge is an individual unless:

(i) after the pledge becomes enforceable, the provider and the secured creditor agree in writing that it may be enforced without such an order, or

(ii) the provider being a sole trader, enforcement is against property used wholly or mainly for the purposes of the provider's business.

(Paragraph 27.54; Draft Bill, s 70(1))

132. (a) The definitions of "dealing" in the Matrimonial Homes (Family Protection) (Scotland) Act 1981 and the Civil Partnership Act 2004 should be amended so as to include the grant of a statutory pledge.

(b) The protections conferred by the Matrimonial Homes (Family Protection) (Scotland) Act 1981 and the Civil Partnership Act 2004 on heritable creditors who have acted in good faith should be amended so as to apply to secured creditors of statutory pledges.

(Paragraph 27.58; Draft Bill, s 58(1) and (7) to (12))

133. (a) Before taking any steps to enforce a statutory pledge the secured creditor should be required to serve a special form of Pledge Enforcement Notice on any occupier of the encumbered property or part of it.

(b) A court order should be required for enforcing a statutory pledge as regards encumbered property which is the sole or main residence of an individual (whether or not the individual is the provider of the security) unless:

(i) after the statutory pledge becomes enforceable the secured creditor, the provider and (if the individual is not the provider) the individual agree otherwise, and

(ii) the agreement is a written agreement.

(c) The court should not grant an order unless satisfied that enforcement is reasonable in all the circumstances of the case.

(d) Those circumstances should include:

(i) the nature of, and reason for, the default by virtue of which authority to enforce is sought,

(ii) whether the person in default has the ability to remedy the default within a reasonable time,

(iii) whether the secured creditor has done anything to remedy the default,

(iv) whether it is, or was, appropriate for the person in default to take part in a debt payment programme approved under Part 1 of the Debt Arrangement and Attachment (Scotland) Act 2002, whether the person in default is taking part, or has taken part, in such a programme, and

(v) whether reasonable alternative accommodation is available for (or can be expected to be available for) the individual whose sole or main residence is the property.

(Paragraph 27.63; Draft Bill, ss 69(1)(e) and 70(2), (4) and (5))

134. The protections conferred by the Matrimonial Homes (Family Protection) (Scotland) Act 1981 and the Civil Partnership Act 2004 in relation to creditors under hire-purchase and conditional sale agreements in relation to furniture and plenishings should be extended to include secured creditors of statutory pledges.

(Paragraph 27.67; Draft Bill, s 58(1) to (6))

135. (a) The following rules should apply in relation to corporeal property in respect of which a secured creditor in a statutory pledge has served a Pledge Enforcement Notice.

(b) The secured creditor should be entitled:

(i) to take possession of the property, or

(ii) to take any reasonable steps necessary to ensure, whether or not by immobilising the property, that it is not disposed of or used in an unauthorised way.

(c) The secured creditor should be able to take such possession, or such steps,

(i) personally if authorised to do so by the court but otherwise only with the consent of the provider given after default, and of any third party who is in direct possession of, or has custody of, the property, or

(ii) through the agency of an authorised person.

(d) The secured creditor should be entitled, in taking possession of the encumbered property to remove any individual from it, but only through the agency of an authorised person.

(e) An "authorised person" should mean:

(i) a messenger-at-arms or sheriff officer,

(ii) a person qualified to act as an insolvency practitioner, or

(iii) such other person as the Scottish Ministers may by regulations specify.

(Paragraph 27.76; Draft Bill, s 71(1) to (4) and (8) to (9))

136. (a) The secured creditor should not have an entitlement to take possession of the encumbered property or to take the steps set out in the previous recommendation if the property is in the possession of a person:

(i) who has a right in security over the property, or over any part of the property, being a right in security which has priority over, or ranks equally with, the pledge to which the Pledge Enforcement Notice relates, or

(ii) who has executed diligence against the property, or against any part of the property, and by virtue of that diligence has priority in ranking over, or ranks equally with, that pledge.

(b) But in these circumstances the secured creditor may take possession or take these steps:

(i) with the consent of the person who has the right in security over the property, or has executed diligence against it,

(ii) if authorised by the court, through the agency of an authorised person, or

(iii) personally, if authorised to do so by the court.

(Paragraph 27.79; Draft Bill, s 71(6) & (7))

137. The taking of possession of financial instrument certificates by the secured creditor should be subject to similar rules as the taking of possession of corporeal property.

(Paragraph 27.81; Draft Bill, s 72)

138. (a) Where a pledge is being enforced, the secured creditor should be entitled to sell all or any of the encumbered property.

(b) The secured creditor, in selling the property, should require to take all reasonable steps to ensure that the price obtained is the best reasonably obtainable.

(c) The secured creditor should be entitled to purchase all or any of the property only if the sale is by public auction and if the price bears a reasonable relationship to market value.

(d) If the property is tradeable in a public market in which the current market value is verifiable the secured creditor should be entitled to purchase all or any of the property only in that market and for market value.

(e) Any proceeds derived from the sale should require to be held in trust until applied by the secured creditor.

(Paragraph 28.8; Draft Bill, s 73)

139. Where the secured creditor sells encumbered property on enforcement the purchaser should acquire the property unencumbered by:

(a) the pledge,

(b) any right in security or any diligence ranking equally with, or postponed to, the pledge, and

(c) any right in security or any diligence which has priority in ranking over the pledge, but only if the holder of that right in security, or as the case may be the creditor who executed that diligence, consented to the sale.

(Paragraph 28.13; Draft Bill, s 74)

140. (a) Where a pledge is being enforced it should be competent for the secured creditor to let all or any of the encumbered property.

(b) The secured creditor in letting the property should require to take all reasonable steps to ensure that the rental income obtained is the best reasonably obtainable.

(c) The rental income obtained should be held in trust by the secured creditor until applied towards the satisfaction of the secured obligation.

(d) The provider and the secured creditor should be able to agree that the right to let is excluded in respect of all or any of the encumbered property. Such an agreement should require to be set out in writing.

(Paragraph 28.15; Draft Bill, s 75)

141. (a) Where a statutory pledge over intellectual property is being enforced it should be competent for the secured creditor to grant a licence over all or any of that property (but only if and to the extent that the provider is entitled to grant such a licence).

(b) The secured creditor in granting a licence should require to take all reasonable steps to ensure that the rental income obtained is the best reasonably obtainable.

(c) The income obtained should be held in trust by the secured creditor until applied towards the satisfaction of the secured obligation.

(d) The provider and the secured creditor should be able to agree that the right to grant a licence is excluded in respect of all or any of the intellectual property encumbered by the statutory pledge. Such an agreement should require to be set out in writing.

(Paragraph 28.18; Draft Bill, s 76)

142. (a) A secured creditor who is enforcing a pledge should be entitled to take reasonable steps to protect, maintain and manage the encumbered property and to preserve its value.

(b) Such steps could include:

(i) exercising any voting rights in relation to a financial instrument which is encumbered property,

(ii) effecting or maintaining an insurance policy in relation to the encumbered property,

(iii) settling any liability in relation to that property,

(iv) bringing, defending or continuing legal proceedings in relation to that property, and

(v) taking such other steps as the provider, whether before or after the pledge has become enforceable, has agreed may be taken by the secured creditor.

(Paragraph 28.20; Draft Bill, s 77)

143. (a) Any proceeds arising from enforcement should be applied:

(i) firstly, in payment of all expenses reasonably incurred by or on behalf of the secured creditor in connection with the enforcement,

(ii) secondly, in payment of the amount due under any right in security over the property from which the proceeds arose, or to a creditor who has executed diligence against that property in accordance with ranking, and

(iii) thirdly, in payment to the provider of any residue.

(b) No payment should be made to a higher ranking creditor unless it has consented to the realisation.

(c) Where payment is to be made to more than one person with the same ranking but the proceeds are inadequate to enable those persons to be paid in full, their payments should abate in equal proportions.

(d) "Expenses" should be defined to include the costs of taking possession of, immobilising and managing the property.

(Paragraph 28.33; Draft Bill, s 82(1) to (5) & (10))

144. (a) Where a question arises as to whom a payment should be made, the secured creditor should be required to:

(i) consign the amount of the payment (so far as ascertainable) in court for the person appearing to have the best right to that payment, and

(ii) lodge in court a statement of the amount consigned.

(b) Such a consignation should operate as a payment of the amount due and a certificate of the court should be sufficient evidence of that payment.

(Paragraph 28.35; Draft Bill, s 82(6) to (9))

145. (a) The secured creditor should be required, as soon as reasonably practicable, to present:

(i) the provider,

(ii) the debtor in the secured obligation if a person other than the provider,

(iii) any other creditor affected by the enforcement, and

(iv) any prescribed person who has statutory duties in relation to the provider's estate

with a written statement of how the proceeds arising from the enforcement have been applied.

(b) But where the proceeds arise from the letting or licensing of the property a monthly statement should be sufficient.

(Paragraph 28.37; Draft Bill, s 82(11) & (12))

146. (a) The secured creditor should be entitled to appropriate any or all of the encumbered property in total or partial satisfaction of the secured obligation.

(b) But it should not be competent to appropriate:

(i) the property of an individual unless that person is a sole trader and the appropriation is of assets used wholly or mainly for the purposes of the person's business,

(ii) corporeal property, or a financial instrument payable to bearer, unless it is in the possession of the secured creditor, or

(iii) property the value of which exceeds the amount for the time being remaining due under the secured obligation and the costs of enforcement unless the secured creditor holds the excess amount on trust to be applied as if it were proceeds.

(Paragraph 28.43; Draft Bill, s 78)

147. (a) Before exercising any right to appropriate property, the secured creditor should require to serve a notice on:

(i) the provider,

(ii) the debtor in the secured obligation if a person other than the provider,

(iii) any other person with a right in security over all or part of the property,

(iv) any person who has executed diligence against all or part of the property, and

(v) any person who has statutory duties in relation to the provider's estate and is prescribed under this paragraph.

(b) But the duty in cases (iii) and (iv) is to be waived if the secured creditor does not know and cannot reasonably be expected to know of the right in security or diligence.

(c) Any notice should require to:

(i) identify the property to be appropriated,

(ii) specify

(a) the amount for the time being remaining due under the secured obligation, and

(b) the amount to be obtained by the appropriation

(iii) state that the recipient has a right to object within 14 days of the receipt of the notice.

(d) The appropriation may not proceed unless the amount to be obtained by it bears a reasonable relationship to the market value of the property.

(e) If within 14 days after receiving notice a recipient, by means of a written statement made to the secured creditor, objects to the appropriation, it is not to proceed.

(Paragraph 28.48; Draft Bill, s 79)

148. (a) The provider and the secured creditor should be able, before the pledge becomes enforceable, to agree in writing that the secured creditor is entitled to appropriate the encumbered property or part of that property.

(b) Any property to be appropriated in accordance with that agreement must be:

(i) a fungible asset that is traded on a specified market, being a market the prices on which are published and widely available (whether on payment of a fee or otherwise) or

(ii) if it is not such an asset so traded, property as regards which the provider and the secured creditor have, in the agreement, set out a method of readily determining a reasonable market price,

and be appropriated only for the value of its market price as so published or as the case may be as so determined.

(c) Notice should require to be given to the same parties as mentioned in the previous recommendation of the proposed appropriation and other than the provider (or debtor where different from the provider) they should have the right to object within 14 days of receiving the notice.

(d) "Fungible asset" should be defined as an asset of a nature to be dealt in without identifying the particular asset involved, and "specified" as specified for these purposes by the Scottish Ministers by regulations. It should be possible for the regulations to specify different markets or descriptions of market in relation to different kinds of fungible asset.

(Paragraph 28.55; Draft Bill, s 80)

149. Where the secured creditor appropriates encumbered property, the property should be acquired unencumbered by any right in security or any diligence.

(Paragraph 28.57; Draft Bill, s 81)

150. Where a statutory pledge is extinguished as a result of it or another right in security over the same property being enforced, or as a result of diligence being executed against that property, the secured creditor should be required, as soon as reasonably practicable, to apply to the Keeper to correct the Register of Statutory Pledges to remove the relevant entry.

(Paragraph 28.58; Draft Bill, s 83)

151. (a) A person should be entitled to be compensated by a secured creditor for loss suffered in consequence of the secured creditor's failure to comply with the statutory obligations imposed on the secured creditor in relation to enforcement.

(b) But the secured creditor should have no liability:

(i) in so far as the loss could have been avoided by the person taking certain measures which it would have been reasonable for the person to take, and

(ii) in so far as the loss is not reasonably foreseeable.

(Paragraph 28.64; Draft Bill, s 85)

152. (a) In respect of the application of section 26 of the Interpretation and Legislative Reform (Scotland) Act 2010 in relation to the service of enforcement notices the provider and the secured creditor should be able to agree that service is to be effected either or both at a specified address and by a specified method.

(b) Such an agreement should require to be in writing.

(c) Where there is such an agreement but service cannot be effected in accordance with it the agreement is to be disregarded.

(Paragraph 28.67; Draft Bill, s 86)

153. A new public register should be established, to be called the Register of Statutory Pledges, in which statutory pledges can be registered.

(Paragraph 29.5; Draft Bill, s 87(1))

154. The register should be under the management and control of the Keeper of the Registers of Scotland.

(Paragraph 29.8; Draft Bill, s 87(2))

155. Where an application is made for registration of a statutory pledge it should require to be accompanied by a copy of the constitutive document.

(Paragraph 29.14; Draft Bill, s 91(2)(a)(ii))

156. A copy of a document amending a registered statutory pledge to add property to the encumbered property or to increase the extent of the secured obligation should require to be registered.

(Paragraph 29.21; Draft Bill, s 92(2)(b))

157. (a) Subject to the requirements of statute, the register should be in such form as the Keeper thinks fit.

(b) The Keeper should take such steps as appear reasonable to her for protecting the register from interference, unauthorised access, or damage.

(Paragraph 29.23; Draft Bill, s 87(3) and (4))

158. Registration in the RSP should be by electronic means only and should be by means of an automated system under which applications are not checked by the Keeper.

(Paragraph 29.24; Draft Bill, s 119)

159. The Keeper should make up and maintain, as parts of the Register of Statutory Pledges:

(a) the statutory pledges record, and

(b) the archive record.

(Paragraph 30.2; Draft Bill, s 88)

160. An entry in the statutory pledges record should comprise:

(a) the provider's name and address,

(b) where the provider is an individual, the provider's date of birth,

(c) any number which the provider bears or other information relating to the provider which, by virtue of RSP Rules, must be included in the entry,

(d) the secured creditor's name and address,

(e) any number which the secured creditor bears or other information relating to the secured creditor which, by virtue of RSP Rules, must be included in the entry,

(f) where the secured creditor is not an individual, an address (which may be an email address) to which requests for information regarding the statutory pledge may be directed,

(g) such description of the encumbered property as may be required or permitted by RSP Rules,

(h) a copy of the constitutive document of the statutory pledge and any amendment document,

(i) the registration number allocated to the entry,

(j) the date and time of registration of the statutory pledge and any amendment to it, and

(k) such other data as may be required by legislation.

(Paragraph 30.10; Draft Bill, s 89(1))

161. (a) An application for registration of a statutory pledge should be made by or on behalf of the secured creditor.

(b) The Keeper should be required to accept an application if:

(i) it conforms to RSP Rules in relation to applications,

(ii) it is submitted with a copy of the constitutive document,

(iii) it provides the Keeper with the necessary data to make up an entry in the RSP, and

(iv) the registration fee is paid or the Keeper is satisfied that it will be.

(c) Where these requirements are not satisfied, the Keeper should be required to reject the application and inform the applicant accordingly.

(Paragraph 30.14; Draft Bill, ss 91(1) to (3) and 118(4))

162. On accepting an application for registration, the Keeper should be required to:

(a) make up and maintain in the statutory pledges record an entry for the statutory pledge, and

(b) allocate a registration number to the entry.

(Paragraph 30.16; Draft Bill, s 91(4))

163. (a) An application for registration of an amendment of a statutory pledge to add property to the encumbered property or to increase the extent of the secured obligation should be made by or on behalf of the secured creditor.

(b) The Keeper should be required to accept an application if:

(i) it conforms to RSP Rules in relation to applications,

(ii) it is submitted with a copy of the amendment document,

(iii) it provides the Keeper with the necessary data to update the entry in the RSP, and

(iv) the registration fee is paid or the Keeper is satisfied that it will be.

(c) Where these requirements are not satisfied, the Keeper should be required to reject the application and inform the applicant accordingly.

(Paragraph 30.18; Draft Bill, ss 92(1) to (3) and 118(4))

164. On accepting an application for registration of an amendment the Keeper should be required to update the entry for the statutory pledge accordingly.

(Paragraph 30.21; Draft Bill, s 92(4))

165. (a) The Keeper should be required to issue a verification statement on accepting an application for registration.

(b) The statement should require to conform to RSP Rules. It should include the date and time of the registration and the unique number allocated to the entry to which the application relates.

(c) The provider should be entitled to request a copy of the verification statement and the secured creditor should be required to supply this within 21 days after the request is made.

(Paragraph 30.24; Draft Bill, s 93)

166. (a) A registration should be taken to be made on the date and time which are entered for it in the Register of Statutory Pledges.

(b) The Keeper should be required to deal with applications for registration and allocate these registration numbers in order of receipt.

(Paragraph 30.25; Draft Bill, s 94)

167. The registration of a statutory pledge should be ineffective if the entry made up for it:

(a) does not include a copy of the constitutive document,

(b) that document is invalid, or

(c) there is an inaccuracy in relation to the data registered which, as at the time of registration, is seriously misleading.

(Paragraph 31.4; Draft Bill, s 95(1))

168. The registration of an amendment to a statutory pledge should be ineffective if:

(a) the entry for the statutory pledge does not include a copy of the amendment document,

(b) that document is invalid, or

(c) there is an inaccuracy in relation to the data registered for the statutory pledge in consequence of the amendment which is seriously misleading.

(Paragraph 31.6; Draft Bill, s 96(1))

169. (a) An inaccuracy in an entry in the statutory pledges record may be seriously misleading irrespective of whether any person has been misled.

(b) In determining whether an inaccuracy is seriously misleading no account should be taken of any document included in the entry.

(c) An inaccuracy which is seriously misleading in respect of part of an entry should not affect the rest of the entry.

(d) Without prejudice to the generality, an inaccuracy should be seriously misleading:

(i) where the provider (or as the case may be, a co-provider) is not a person required by RSP Rules to be identified by a unique number, if a search using a designated facility provided for by the Keeper for:

(a) the provider's (or co-provider's) proper name, or

(b) the provider's (or co-provider's) proper name and the provider's (or co-provider's) date of birth)

does not disclose the entry,

(ii) where the provider (or, as the case may be, co-provider) is a person required by RSP Rules to be identified by a unique number, if a search using a designated facility provided for by the Keeper for that number does not disclose the entry, including where a search using such a facility for the provider's (or co-provider's) number does disclose the entry,

(iii) in respect of so much of the encumbered property as bears a unique number which must, by virtue of RSP Rules, be included in the statutory pledges record, if a search using a designated facility provided for by the Keeper for that number does not disclose the entry.

(e) The meaning of "proper name" should be set out in RSP Rules.

(f) The Scottish Ministers should be able to specify further instances in which an inaccuracy is seriously misleading.

(Paragraph 31.18; Draft Bill, s 98)

170. (a) Where:

(i) a statutory pledge is effectively registered over property,

(ii) at some time after that registration either

(a) the relevant entry in the statutory pledges record comes to contain an inaccuracy which is seriously misleading (whether or not in respect of all the encumbered property), or

(b) is removed from that record, and

(iii) prior to any correction being effected a person acquires, for value and in good faith while exercising reasonable care,

(a) all or part of the encumbered property, or

(b) a right in, or in part of, that property

the statutory pledge should be extinguished, but in the case of an inaccuracy only as regards so much of the property acquired as is property in respect of which the inaccuracy is seriously misleading.

(b) This rule should not apply where there is an inaccuracy in an entry but the property acquired is of a prescribed type and the unique number for the property appears in the entry.

(Paragraph 32.51; Draft Bill, s 97)

171. Except in so far as the context otherwise requires any reference to "correction" should include correction by:

(a) the removal of data included in an entry,

(b) the removal of an entry from the statutory pledges record and the transfer of that entry to the archive record,

(c) the replacement of data, or of a copy document, included in an entry,

(d) the restoration of data, or of a copy document, to an entry, or

(e) the restoration of an entry (whether or not by removing it from the archive record and transferring it to the statutory pledges record).

(Paragraph 33.5; Draft Bill, s 105(1))

172. (a) Where the Keeper becomes aware of a manifest inaccuracy in an entry in the statutory pledges record the Keeper should have to correct the inaccuracy if what is needed to correct it is manifest. If what is needed to correct is not manifest the Keeper should have to note the inaccuracy on the entry.

(b) Where an inaccuracy is corrected by:

(i) removal of the entry the Keeper should have to transfer the entry to the archive record and note on the entry the details of the correction, and its date and time,

(ii) removal or replacement of data included in the entry or by replacement of a copy document the Keeper should have to note on the entry the details of the correction, and its date and time,

(iii) replacement of a copy document, the Keeper should have to transfer it to the archive record.

(c) Where the Keeper effects a correction, the Keeper should have to notify each person specified for these purposes by RSP Rules and any other person whom the Keeper considers it appropriate to notify that the correction has been effected.

(Paragraph 33.7; Draft Bill, s 102)

173. (a) Where a court determines that the statutory pledges record is inaccurate it should have the power to direct the Keeper to correct it.

(b) In connection with any such correction, the court should be able to give the Keeper such further direction (if any) as it considers requisite.

(c) The Keeper should be required to note in the relevant entry that it has been corrected and the details of the correction, including the date and time. Where the correction requires the removal of the entry or of a copy document the Keeper should have to transfer it to the archive record.

(d) Where the Keeper effects a correction, the Keeper should have to notify each person specified for these purposes by RSP Rules and any other person whom the Keeper considers it appropriate to notify that the correction has been effected.

(Paragraph 33.9; Draft Bill, s 103)

174. The Keeper should be entitled to appear and be heard in any civil proceedings, whether before a court or tribunal, in which is put in question (either or both):

(a) the accuracy of the statutory pledges record,

(b) what is needed to correct an inaccuracy in that record.

(Paragraph 33.10; Draft Bill, s 104)

175. (a) The secured creditor should be able to apply for correction of the entry for the statutory pledge in the statutory pledges record.

(b) The Keeper should be required to accept an application if it conforms to RSP Rules in relation to applications and the prescribed fee is paid or the Keeper is satisfied that it will be.

(c) Where these requirements are not satisfied, the Keeper should be required to reject the application and inform the applicant accordingly.

(d) On accepting an application for correction of the statutory pledges record the Keeper should be required to correct the entry accordingly, and issue to the applicant and to the provider of the statutory pledge a written statement verifying the correction.

(e) The verification statement should conform to such RSP Rules as may relate to the statement and include both the date and time of the correction and the registration number allocated to the entry to which the application relates.

(f) The Keeper should be required to note on the relevant entry that it has been corrected and the details of the correction, including the date and time. Where the correction requires the removal of the entry the Keeper should have to transfer it to the archive record.

(Paragraph 33.22; Draft Bill, s 100)

176. (a) A person who:

(i) is identified incorrectly as the provider, or as a co-provider, of a statutory pledge in an entry in the statutory pledges record, or

(ii) holds a right in property identified incorrectly as the encumbered property in an entry in the statutory pledges record

may issue a demand in a prescribed form to the person identified in the entry as the secured creditor that the person so identified apply to the Keeper for correction of the statutory pledges record.

(b) Such a demand should require to specify a period (being not less than 21 days after it is received) within which it must be complied with.

(c) No fee may be charged by the person identified as the secured creditor for such compliance.

(d) Where the demand is not complied with the person making it should be able to apply to the Keeper for the correction.

(e) The application should require to conform to such RSP Rules as may relate to it.

(f) On receiving an application the Keeper should be required to:

(i) serve a notice on the person identified in the entry as the secured creditor stating that the Keeper will correct the record on a date specified in the notice (being a date no fewer than 21 days after the date of the notice),

(ii) note on the relevant entry that an application has been received and include in that note the details of the correction sought and the date of receipt,

(iii) issue to the applicant a written statement verifying that the application has been received, and

(iv) notify the person identified in the entry as the provider (if a different person from the applicant) that the notice mentioned in (i) has been served.

(g) The person identified as the secured creditor should have the right to apply to the court prior to the date specified in the notice to oppose the making of the correction and on making any such application should have to notify the Keeper.

(h) The court should be able to direct whether the entry should be corrected or left unchanged, but only if satisfied that the Keeper has been notified of the application to the court prior to the date specified in the notice.

(i) If the Keeper does not receive such notification prior to the date specified in the notice, the Keeper should be required to make the correction on that date.

(j) The Keeper should be required to note in the relevant entry that it has been corrected and the details of the correction, including the date and time. Where the correction requires the removal of the entry the Keeper should have to transfer it to the archive record.

(k) Where the Keeper effects a correction, the Keeper should have to notify each person specified for these purposes by RSP Rules and any other person whom the Keeper considers it appropriate to notify that the correction has been effected.

(Paragraph 33.34; Draft Bill, s 101)

177. A registration which is ineffective should become effective if and when the entry is corrected.

(Paragraph 33.37; Draft Bill, ss 95(3) and 96(3))

178. A correction should be taken to be made on the date and at the time which are entered for it in the register.

(Paragraph 33.38; Draft Bill, s 105(2))

179. The statutory pledges record should be searchable only:

(a) by reference to any of the following data in the entries contained in that record:

(i) the names of providers,

(ii) the names and dates of birth of providers who are individuals,

(iii) the unique numbers of providers required by RSP Rules to be identified in the statutory pledges record by such a number,

(b) if RSP Rules require or permit the encumbered property to be identified by a unique number by reference to that number,

(c) by reference to registration numbers allocated to entries in that record, or

(d) by reference to some other factor, or characteristic, specified for these purposes by RSP Rules.

(Paragraph 34.7; Draft Bill, s 106(2))

180. A person should be able to search the statutory pledges record if the search accords with RSP Rules and either such fee as is payable for the search is paid or the Keeper is satisfied that it will be paid.

(Paragraph 34.9; Draft Bill, s 106(1))

181. (a) The Keeper should be required to provide a search facility in relation to which the search criteria are specified by RSP Rules, but may provide such other search facilities, with such other search criteria, as the Keeper thinks fit.

(b) "Search criteria" should be defined as the criteria in accordance with which what is searched for must match data in an entry in order to retrieve the entry.

(Paragraph 34.11; Draft Bill, s 107)

182. A printed search result which purports to show an entry in the statutory pledges record:

(a) should be admissible in evidence, and

(b) in the absence of evidence to the contrary, should be sufficient proof of:

(i) the registration of the statutory pledge, or amendment to the entry in the statutory pledges record, to which the result relates,

(ii) a correction of the entry in the statutory pledges record to which the result relates, and

(iii) the date and time of such registration or correction.

(Paragraph 34.13; Draft Bill, s 108)

183. (a) Any person should be able to apply to the Keeper for an extract of an entry in the register.

(b) The Keeper should be required to issue the extract if such fee as is payable for issuing it is paid or arrangements satisfactory to the Keeper are made for payment of that fee.

(c) The Keeper should be able to validate the extract as the Keeper considers appropriate.

(d) The Keeper should be able to issue the extract as an electronic document if the applicant does not require that it be issued as a traditional document.

(e) The extract should be accepted for all purposes as sufficient evidence of the contents, as at the date on which and time at which the extract is issued (being a date and time specified in the extract).

(Paragraph 34.15; Draft Bill, s 109)

184. (a) An entitled person should be entitled to request from the person identified in an entry in the statutory pledges record as the secured creditor:

(i) if that person is the secured creditor, a written statement:

(a) as to whether or not property specified by the entitled person is, or is part of, the encumbered property; or

(b) describing the secured obligation, or

(ii) if that person has assigned the statutory pledge, the name and address of the assignee and (as the case may be and in so far as known) the names and addresses of subsequent assignees.

(b) The following should be entitled persons:

(i) a person who has a right in the property so specified,

(ii) a person who has the right to execute diligence against that property (or who is authorised by decree to execute a charge for payment and will have the right to execute diligence against that property if and when the days of charge expire without payment),

(iii) a person who is prescribed for these purposes, and

(iv) a person who has the consent of the person identified in the entry as the provider.

(Paragraph 35.8; Draft Bill, s 110(1) to (2))

185. (a) An information request should require to be complied with within 21 days of its receipt, unless:

(i) the court is satisfied that in all the circumstances this would be unreasonable and either extends the 21-day period or exempts the recipient from complying with the request in whole or in part,

(ii) it is manifest from the entry that the property specified in the notice has not been encumbered by the statutory pledge or that the registration is ineffective,

(iii) where a request has been made for a description of the secured obligation where it is manifest from the entry alone what the extent of that obligation is, or

(iv) the same request has been made by the same person within the last 3 months and the information supplied in response to the last request has not changed.

(b) The recipient should be entitled to recover from the requester any costs reasonably incurred in complying with the request.

(c) If the court is satisfied on the application of the requester that the recipient has not complied with the duty to provide information without reasonable excuse it should by order require that the recipient complies within 14 days.

(Paragraph 35.14; Draft Bill, s 110(3) to (7))

186. Where:

(a) an entitled person in response to an information request is incorrectly informed that the property specified in the request is unencumbered by the statutory pledge, and

(b) within 3 months of being so informed acquires in good faith

(i) the property so specified or any part of it,

(ii) a right in that property (or any part of it),

on the acquisition the statutory pledge is extinguished as regards the property or part.

(Paragraph 35.18; Draft Bill, s 110(8) to (9))

187. The duties to provide information should also apply to any assignee of the statutory pledge.

(Paragraph 35.19; Draft Bill, s 110(10))

188. (a) The Scottish Ministers should have power to make regulations specifying a period after which an entry in the statutory pledges record will lapse unless it is renewed.

(b) Before exercising this power, the Scottish Ministers must consult the Keeper.

(Paragraph 35.29; Draft Bill, s 99)

189. The archive record should be the totality of all the entries transferred from the statutory pledges record following:

(a) correction to remove an entry, and

(b) lapsing of a statutory pledge under regulations made by the Scottish Ministers,

and should also contain such other information as may be specified by RSP Rules.

(Paragraph 35.32; Draft Bill, s 90)

190. (a) A person should be entitled to be compensated by the Keeper for loss suffered in consequence of:

(i) an inaccuracy attributable to the Keeper in the making up, maintenance or operation of the Register of Statutory Pledges, or in an attempted correction of the register,

(ii) the issue of a statement or notification which is incorrect, or

(iii) the issue of an extract which is not a true extract.

(b) But the Keeper should have no statutory liability:

(i) in so far as the person's loss could have been avoided had the person taken measures which it would have been reasonable for the person to take,

(ii) in so far as the person's loss is not reasonably foreseeable, or

(iii) for non-patrimonial loss.

(Paragraph 35.34; Draft Bill, s 111)

191. (a) Where a person suffers loss in consequence of:

(i) an inaccuracy in an entry in the Register of Statutory Pledges (which is not caused by the Keeper), the person should be entitled to be compensated for that loss by the person who made the application which gave rise to that entry if, in making it, that person failed to take reasonable care, or

(ii) a failure to respond to a request for information under the information duty provisions, or the provision of information in which there is an inaccuracy, the person is entitled to be compensated for that loss by the person who failed to supply the information if that failure was without reasonable cause or if, in supplying it, that person failed to take reasonable care.

(b) But there should be no liability:

(i) in so far as the person's loss could have been avoided had the person taken measures which it would have been reasonable for the person to take,

(ii) in so far as the loss is not reasonably foreseeable, or

(iii) for non-patrimonial loss.

(Paragraph 35.36; Draft Bill, s 112)

192. The Scottish Ministers should, following consultation with the Keeper, be able by regulations to make rules (to be known as "RSP Rules"):

(a) as to the making up and keeping of the register,

(b) as to procedure in relation to applications:

(i) for registration, or

(ii) for corrections,

(c) as to the identification, in any such application of any person or property, including:

(i) how the proper form of a person's name is to be determined, and

(ii) where the person bears a number (whether of numerals or of letters and numerals) unique to the person, whether that number must (or may) be used in identifying the person,

(d) as to the degree of precision with which time is to be recorded in the register,

(e) as to the manner in which an inaccuracy in the statutory pledges record may be brought to the attention of the Keeper,

(f) as to information which, though contained in a constitutive document or amendment document, need not be included in a copy of that document submitted with an application for registration,

(g) as to whether a signature contained in a constitutive document or amendment document need be included in a copy of that document so submitted,

(h) as to searches in the register,

(i) as to information which, though contained in the register, is not to be –

(i) available to persons searching it, or

(ii) included in any extract issued by the Keeper,

(j) prescribing the configuration, formatting and content of:

(i) applications,

(ii) notices,

(iii) documents,

(iv) data,

(v) statements, and

(vi) requests

to be used in relation to the register,

(k) as to when the register is open for:

(i) registration, and

(ii) searches,

(l) requiring there to be entered in the statutory pledges record or the archive record such data as may be specified in the rules, or

(m) regarding other matters in relation to registration, being matters for which the Scottish Ministers consider it necessary or expedient to give full effect to the purposes of the draft Bill.

(Paragraph 35.38; Draft Bill, s 114)

193. A statutory pledge granted by a company should be registered in both the Register of Statutory Pledges and the Companies Register, but the possibility of an order being made under the Companies Act 2006 section 893 should be kept under review.

(Paragraph 36.28)

194. The creation of a statutory pledge over a financial instrument should require either:

(a) registration in the Register of Statutory Pledges and compliance with the ordinary rules for creation of statutory pledges, or

(b) in a case where a constitutive document or amendment document evidences a security financial collateral arrangement in respect of the instrument, the satisfaction of the following criteria:

(i) the financial instrument to be the property of the provider,

(ii) the financial instrument to have come into the possession of, or under the control of, the collateral-taker or a person acting on the collateral-taker's behalf, and

(iii) identification of the financial instrument as one to which the constitutive document or amendment document relates.

(Paragraph 37.5; Draft Bill, s 50(1)–(3) & (6))

195. Where a statutory pledge over a financial instrument is created without registration:

(a) there should be no requirement for it to be executed or signed electronically, and

(b) the constitutive document and any amendment document may be evidenced by writing transcribed by electronic or other means in a durable medium, or as sounds recorded in such a medium.

(Paragraph 37.5; Draft Bill, s 50(4) to (6))

196. Where a statutory pledge over a financial instrument is created without registration:

(a) it may be assigned by an evidenced agreement between the collateral-taker and the assignee, and

(b) that agreement may be evidenced in writing transcribed by electronic or other means in a durable medium, or in sounds recorded in such a medium.

(Paragraph 37.6; Draft Bill, ss 59(3) and 63)

197. Where a statutory pledge over a financial instrument is created without registration:

(a) it may be amended by an evidenced agreement between the collateral-taker and the provider, and

(b) that agreement may be evidenced in writing transcribed by electronic or other means in a durable medium, or in sounds recorded in such a medium.

(Paragraph 37.7; Draft Bill, ss 60(8) and 63)

198. (a) A statutory pledge created as a security financial collateral arrangement without registration in the Register of Statutory Pledges should be:

(i) extinguished in relation to the financial instrument over which the pledge is created on the financial instrument ceasing to be in the

possession, or under the control, of the collateral-taker or of a person acting on behalf of the collateral- taker, or

(ii) restricted to only part of the encumbered property by means of an evidenced statement of the collateral-taker.

(b) Such a statement may be evidenced in writing transcribed by electronic or other means in a durable medium, or sounds recorded in such a medium.

(Paragraph 37.10; Draft Bill, ss 62 and 63)

199. Nothing in the enforcement rules for pledge should be taken to derogate from such rights as a secured creditor may have by virtue of Part 4 of the Financial Collateral Arrangements (No. 2) Regulations 2003 (right of use and appropriation).

(Paragraph 37.14; Draft Bill, s 84)

200. The recommendation of the Murray Report that sole traders and ordinary partnerships should be able to grant floating charges should not now be taken forward.

(Paragraph 38.4)

201. Floating charges should continue to be capable of encumbering immoveable/heritable property.

(Paragraph 38.6)

202. The ranking rules of Scottish floating charges in relation to negative pledge clauses should not be reformed.

(Paragraph 38.9)

203. It should no longer be competent for agricultural charges to be created.

(Paragraph 38.15; Draft Bill, s 115)

Appendix

List of Respondents, Advisory Group members and those who have provided assistance

I. RESPONDENTS TO THE DISCUSSION PAPER

We received written comments on the Discussion Paper (DP No 151) from the following (whose titles and affiliations are given as at the time of the response)

Aberdeen Law School (Professor David Carey Miller and Malcolm Combe)

Dr Ross Anderson, University of Glasgow

Asset Based Finance Association

Dr Jan Biemans, De Brauw Blackstone Westbroek

Begbies Traynor (Ken Patullo CA and Paul Dounis CA)

Brodies LLP (Bruce Stephen, Michael Stoneham)

Professor Stewart Brymer, Brymer Legal Ltd

Civil Aviation Authority

David Cabrelli, University of Edinburgh

Colin Campbell, University of Edinburgh

Committee of Scottish Clearing Bankers

CBI Scotland

Department for Business, Innovation and Skills

Professor Eric Dirix, KU Leuven

Chris Dun, Maclay Murray & Spens LLP

Dundas & Wilson LLP (Andrew Hinstridge, Claire Massie, Caryn Penley, Stephen Phillips, Dawn Reoch)

Faculty of Advocates

Federation of Small Businesses

David Gibson, Burness LLP

David Hill CA, BDO Stoy Hayward

Tom Hughes CA, Gerber Landa Gee Ltd

Institute of Chartered Accountants of Scotland and R3: Association of Business Recovery Professionals

Judges of the Court of Session

Keeper of the Registers of Scotland

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Professor Gerry McCormack, University of Leeds

McGrigors LLP (Gillian Frew, Iain Macaulay, John Macfarlane, Michael Watson)

Donald McGruther CA, Mazars LLP

Jim McLean, Solicitor

Dr Hamish Patrick, Tods Murray LLP

Magadelena Raczynska, University of East Anglia

Dr Andreas Rahmatian, University of Glasgow

Michael Royden, Thorntons LLP

Scottish Council for Development and Industry

Professor Susan Scott, University of South Africa

WS Society

Scott Wortley, University of Edinburgh

II. RESPONDENTS TO THE DRAFT BILL CONSULTATION

We received written comments from the following in response to our consultation on our draft Moveable Transactions (Scotland) Bill of July 2017.

Dr Craig Anderson, Robert Gordon University

Professor Hugh Beale QC, University of Warwick and Professor Louise Gullifer, University of Oxford

Burness Paull LLP

Richard Calnan, Financial Law Committee of the City of London Law Society

Faculty of Advocates

Professor George Gretton, University of Edinburgh

Institute of Chartered Accountants of Scotland

Law Society of Scotland

Dr Hamish Patrick, Shepherd & Wedderburn LLP

R3: Association of Business Recovery Professionals

III. ADVISORY GROUP MEMBERS

As the project progressed, additional members joined the group, which ultimately consisted of:

Dr Ross Anderson, Advocate

Grant Barclay

Morag Campbell, Dentons

Neil Campbell, Shepherd & Wedderburn LLP

Chris Dun, Brodies LLP

The Rt Hon Lord Drummond Young, Court of Session

Gillian Frew, Pinsent Masons LLP

David Gibson, BTO Solicitors LLP

Professor George Gretton, University of Edinburgh

Andrew Hinstridge, Clydesdale Bank

Andrew Kinnes, Shepherd & Wedderburn LLP

Dr John MacLeod, University of Glasgow

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Scott McGeachy, DWF LLP

Dr Hamish Patrick, Shepherd & Wedderburn LLP

Stephen Phillips, CMS Cameron McKenna Nabarro Olswang LLP

Bruce Stephen, Brodies LLP

Bruce Wood, Morton Fraser LLP

Scott Wortley, University of Edinburgh

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Professor Mike Gedye, University of Auckland

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Susan Sutherland

Dr Sean Thomas, University of Durham

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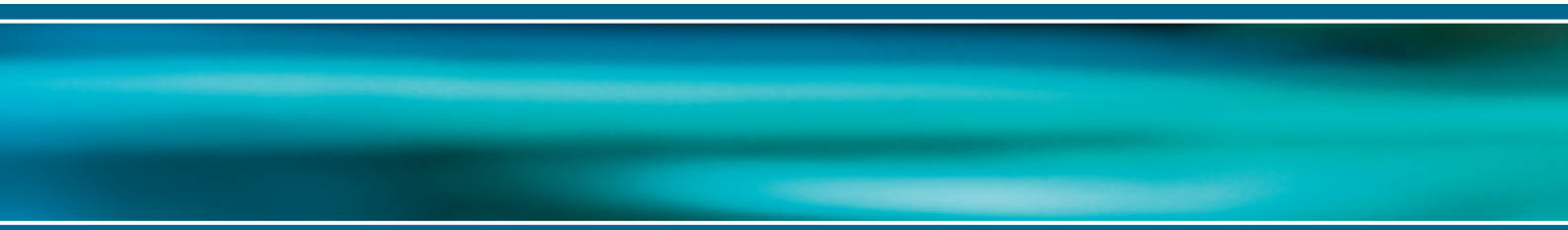
Professor Peter Winship, Southern Methodist University



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Scottish Law Commission

promoting law reform

(SCOT LAW COM No 249)

Report on Moveable Transactions
Volume 3: Draft Bill

report

Scottish Law Commission
promoting law reform

Report on Moveable Transactions Volume 3: Draft Bill

This Report is published in three volumes

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December 2017

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The Scottish Law Commission was set up by section 2 of the Law Commissions Act 1965 (as amended) for the purpose of promoting the reform of the law of Scotland. The Commissioners are:

The Honourable Lord Pentland, *Chairman*
Caroline Drummond
David Johnston QC
Professor Hector L MacQueen
Dr Andrew J M Steven.

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NOTES

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Moveable Transactions (Scotland) Bill

[DRAFT]

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MOVEABLE TRANSACTIONS (SCOTLAND) BILL

[DRAFT]

An Act of the Scottish Parliament to make new provision as regards the assignation of claims; to establish a register of such assignations; to make new provision as regards the granting of security over corporeal and incorporeal moveable property; to establish a register of statutory pledges; to end the creation of agricultural charges; and for connected purposes.

PART 1

ASSIGNATION

CHAPTER 1

ASSIGNATION OF CLAIMS, PROTECTION OF DEBTORS AND RELATED MATTERS

Assignation of claims

1 Assignation of claims: general

(1) The assignation of a claim requires that a document assigning it (in this Act referred to as an "assignation document") be executed or authenticated by the person by whom it is assigned.

(2) In this Part the person—

(a) by whom a claim is assigned, is referred to as the "assignor",

(b) to whom a claim is assigned, is referred to as the "assignee", and

(c) against whom a claim may be enforced, is referred to as the "debtor".

(3) The assignation document must identify the claim.

(4) An assignation document which assigns a number of claims need not identify each claim separately provided that the document identifies the claims in terms of their constituting an identifiable class.

(5) It is competent to assign a claim which, as at the time the assignation document is granted, is not held by the assignor (whether or not the claim yet exists at that time).

(6) Subsection (1) is subject to section 4(4).

NOTE

Subsection (1) has the effect that a claim must be assigned by means of a document ("assignation document"). See section 42(2) of the Bill for the meaning of "claim".

Subject to the exception in subsection (6), the assignation document must be signed by or on behalf of the person assigning the claim either in ink if a hard copy ("executed") or with an electronic signature if an e-

document ("authenticated"). See section 118(1) of the Bill for the meanings of "executed" and "authenticated".

The exception in subsection (6) relates to an assignation for the purpose of a financial collateral arrangement. The requirement in subsection (1) for the assignation document to be executed or authenticated does not apply to assignations for that purpose: see section 4(2)(a) of the Bill in that respect.

Subsection (2) defines the terms "assignor", "assignee" and "debtor" for the purposes of Part 1 of the Bill. The assignor is the person assigning the claim, and the debtor is the person against whom the obligation is enforceable (the person to whom the obligation must be performed is also described in the Bill as the "holder" of the claim). The assignee is the person to whom the claim is assigned (who becomes the new holder).

Subsection (3) requires the claim to be identified, but subsection (4) makes it clear that claims do not need to be individually identified in the assignation document provided that these fall within an identifiable class that is identified. Thus, for example, it would be possible for a business to assign all invoices raised against a particular customer, or all invoices rendered in a period specified in the assignation document.

Subsection (5) confirms that a claim that is not held by the assignor at the date of the assignation, including a claim that has not yet come into being, can be assigned. See paragraphs 5.81 to 5.97 of the Report.

Under the existing law, the requirement of intimation to the debtor makes it difficult to assign such "future" claims. For example, a plumbing business may wish to assign to a factor the invoices for work not yet instructed by a customer. It is not possible to complete the assignation by intimating such a claim until the work had been done, and the debtor can be identified. The alternative method of registration in the Register of Assignations as set up under section 19 of the Bill will however enable the assignation of future claims.

See in general paragraphs 4.6 to 4.30 of the Report.

2 Assignation of claim subject to a condition

(1) An assignation of a claim may be subject to a condition which must be satisfied before the claim is transferred.

(2) Any such condition must be specified in the assignation document.

(3) Without prejudice to the generality of subsection (2), such specification may include making reference to another document the terms of which are not reproduced in the assignation document.

(4) Without prejudice to the generality of subsection (1), the condition referred to in that subsection may be one which depends—

(a) on something happening (whether it is certain or not that the thing will happen), or

(b) on a period of time elapsing during which something must not happen (whether it is certain or not that the thing will happen at some time).

NOTE

This section makes it clear that an assignation can be made subject to a condition which must be satisfied before the claim is transferred, often referred to as a "suspensive condition".

Subsection (2) requires that the condition is set out in the assignation document, in order to enable a third party to be able to discover from the document whether there is such a condition (and in the case of a registered assignation a copy of the document will be included in the assignations record).

Subsection (3) enables a condition to be specified by reference to another document, for example the loan agreement that relates to an assignation in security.

Subsection (4) clarifies that a condition may relate to a thing that will happen, or to a thing that must not happen (in either case regardless of whether or not it is certain that the thing will happen). There is a lack of authority in those respects under the law as it stands before this provision comes into force.

See paragraphs 5.73 to 5.80 of the Report.

3 Transfer of claims

(1) A claim is transferred on the requirements mentioned in subsection (2) all being met.

(2) Those requirements are that—

(a) the assignor is holder of the claim,

(b) either—

(i) intimation of the assignation is effected under section 9(1), or

(ii) the assignation document is registered,

(c) the claim is identifiable as a claim to which the assignation document relates, and

(d) if the assignation is subject to a condition such as is mentioned in section 2(1), the condition is satisfied.

(3) Any rule of law as to accretion is to be disregarded in determining any matter which relates to the transfer, by virtue of subsection (1), of a claim such as is mentioned in section 1(5).

(4) Subsection (1)—

(a) is without prejudice to section 1(1), and

(b) is subject to subsection (6) and to section 4(2)(a).

(5) Subsection (2)(b)(ii) is subject to section 26.

(6) Types of claim may be prescribed in relation to which sub-paragraph (i) of subsection (2)(b) is to be disregarded.

NOTE

This section provides, together with section 4(2)(a), for the transfer to the assignee (the new holder) of an assigned claim.

Subsection (1) provides that a claim is transferred when the four conditions in subsection (2) are all met.

Subsection (2) has the effect that a claim will transfer when:

(a) The assignor is the holder of the claim,

(b) The assignation is intimated (see section 9 of the Bill), or registered in the Register of Assignations (see Chapter 2 of Part 1 of the Bill),

(c) The claim is identifiable as a claim to which the assignation document relates, and

(d) Any condition to which the assignation is subject is met.

It follows that if a claim is not identifiable then the transfer is postponed until it becomes so identifiable.

Example 1 Arthur assigns to Barbara his claim to a current debt of £1000 owed by Zoe. Barbara registers the assignation in the RoA. The claim transfers on registration because the claim as constituted by the debt exists and is clearly identifiable.

Example 2 Debra assigns to Excellent Factors claims in respect of customer invoices to be issued by her as described in schedules to be sent from time to time to the factors. Excellent Factors registers the assignation in advance of any such schedule being sent. There is no transfer at the date of registration as no claim can be identified (and might not exist). The claims listed in the first such schedule transfer when that schedule is issued as they exist and can be identified at that time.

Subsection (3) provides that any rule of law as to accretion is to be disregarded in determining any matter which relates to the transfer of such claims as are mentioned in section 1(5) of the Bill (assignation of a claim not yet held by the assignor).

A person cannot convey property which that person does not own (*nemo dat quod non habet*). Accretion may however operate where a person, who has purported to do so, subsequently acquires the property. See paragraphs 5.98 to 5.100 of the Report.

The effect of accretion would be to cure the defect in the title of the assignee. It is however not clear that accretion applies where "future" claims are assigned, so subsection (3) clarifies that it does not, with the effect that the measures in the Bill replace any common law rule.

Subsections (4) and (5) provides for four qualifications as regards the transfer of claims under this section:

(a) The first qualification has the effect that the assignation document must be formally valid.

(b) The second qualification relates to subsection (6), which enables the Scottish Ministers to prescribe certain categories of claim which can only transfer by registration.

(c) The third qualification relates to financial collateral arrangements, with the effect that a claim may also transfer in accordance with section 4(2)(a) of the Bill.

(d) The fourth qualification concerns registration, with the effect that a claim is only transferred by a registration which is an effective registration for the purposes of section 26 of the Bill.

Subsection (6) enables the Scottish Ministers to prescribe certain categories of claim which can only be transferred by registration of the assignation. For example, in some jurisdictions, assignments in respect of invoices that have yet to be paid must be registered to have third party effect. If registration of assignments of so-called trade receivables was to become required in England and Wales then there may be support for this to be the position in Scotland as well.

See paragraph 5.22 of the Report.

4 Financial collateral arrangements

(1) Subsection (2) applies if an assignation document evidences a security financial collateral arrangement or a title transfer financial collateral arrangement in respect of a claim.

(2) The claim is transferred either—

(a) on the requirements mentioned in subsection (3) all being met, or

(b) as mentioned in section 3(1).

(3) Those requirements are that—

(a) the assignor is holder of the claim,

(b) the financial collateral in question is in the possession, or under the control, of the collateral-taker or of a person authorised to act on the collateral-taker's behalf,

(c) the claim is identifiable as a claim to which the assignation document relates, and

(d) if the assignation is subject to a condition such as is mentioned in section 2(1), the condition is satisfied.

(4) If the claim is transferred by virtue of subsection (2)(a), the requirements of section 1(1) as to execution or authentication do not apply.

(5) Any rule of law as to accretion is to be disregarded in determining any matter which relates to the transfer, by virtue of subsection (2)(a), of a claim such as is mentioned in section 1(5).

(6) Without prejudice to the generality of subsection (1), for the purposes of that subsection the assignation document may, in the case of a claim transferred by virtue of subsection (2)(a), be created—

(a) as writing transcribed by electronic or other means in a durable medium, or

(b) as sounds recorded in such a medium.

(7) This section is to be construed as one with regulation 3 of the Financial Collateral Arrangements (No. 2) Regulations 2003 (S.I. 2003/3226).

NOTE

This section provides for an alternative method for the transfer of a claim where the assignation evidences a financial collateral arrangement.

EU law requires that assignations of that kind are capable if desired of being constituted with only minimum formalities: see Directive 2002/47/EC on Financial Collateral Arrangements, which is transposed for the UK by the Financial Collateral Arrangements (No. 2) Regulations 2003 (S.I. 2003/3226).

A financial collateral arrangement includes both a security financial collateral arrangement and a title transfer financial collateral arrangement, each as defined in the 2003 Regulations (for which see subsection (7)).

Subsections (1) and (2) have the effect that a "financial collateral" claim will transfer either by intimation or registration under section 3 of the Bill, or under the exception for such a claim as provided for by subsection (3).

Subsection (3) has the effect that a "financial collateral" claim will also transfer when all four of the following conditions are met:

(a) The assignor is the holder of the claim,

(b) The collateral in question is in the possession, or under the control of, the collateral-taker (the assignee),

(c) The claim is identifiable as a claim to which the assignation document relates, and

(d) Any condition to which the assignation is subject is met.

Subsection (4) gives effect to Directive 2002/47/EC by providing that the requirements as to execution or authentication of the assignation document in section 1 of the Bill do not apply to a "financial collateral" claim.

Subsection (5) provides that any rule of law as to accretion is to be disregarded, for which see the notes to section 3 of the Bill.

Subsection (6) gives further effect to Directive 2002/47/EC by providing that the assignation document may be created by writing transcribed by electronic or other means in a durable medium, or by sounds recorded in such a medium. That might include the saving of a document, or the recording of a conversation, on a computer hard drive.

See paragraph 14.43, and Chapter 14 generally, of the Report.

5 Assignation of claims: insolvency

(1) Subsection (2) applies where, after an assignation document is granted, the assignor becomes insolvent.

(2) The assignation is ineffective as regards any claim which, though identified by the assignation document as a claim assigned, is not held by the assignor before the assignor becomes insolvent.

(3) Subsection (2) is subject to subsection (8).

(4) For the purposes of this section—

(a) an assignor who is an individual, or the estate of which may be sequestrated by virtue of section 6 of the Bankruptcy (Scotland) Act 2016, becomes insolvent when—

(i) the assignor's estate is sequestrated,

(ii) the assignor grants a trust deed for creditors or makes a composition or arrangement with creditors,

(iii) a voluntary arrangement proposed by the assignor is approved, or

(iv) the assignor's application for a debt payment programme is approved under section 2 of the Debt Arrangement and Attachment (Scotland) Act 2002, and

(b) an assignor other than is mentioned in paragraph (a) becomes insolvent when—

(i) a decision approving a voluntary arrangement entered into by the assignor has effect under section 4A of the Insolvency Act 1986,

(ii) the assignor is wound up under Part 4 or 5 of that Act of 1986 or under section 367 of the Financial Services and Markets Act 2000,

(iii) an administrative receiver, as defined in section 251 of that Act of 1986, is appointed over all or part (being a part which includes the claim) of the property of the assignor, or

(iv) the assignor enters administration ("enters administration" being construed in accordance with paragraph 1(2) of schedule B1 of that Act of 1986).

(5) Subsection (6) applies where a person who has assigned a claim such as is mentioned in section 1(5) is discharged—

(a) under section 137, 138 or 140 of the Bankruptcy (Scotland) Act 2016, or

(b) by virtue of section 184(3) of that Act.

(6) The assignation is ineffective, as regards the claim, if by the time of discharge the assignor has not become the holder of the claim.

(7) The Scottish Ministers may by regulations—

(a) amend—

(i) any sub-paragraph of subsection (4)(a) or (b) (including any sub-paragraph added by virtue of sub-paragraph (ii)), or

(ii) subsection (4)(a) or (b) by adding sub-paragraphs which specify further circumstances in which a person becomes insolvent, or

(b) amend subsections (5) and (6) by specifying further circumstances by reference to which an assignation is to be ineffective as regards a claim.

(8) Subsection (2) does not apply as regards a claim in respect of income from property in so far as that claim—

(a) is not attributable to anything agreed to by, or done by, the assignor after the assignor became insolvent, and

(b) relates to the use of property in existence at the time the assignor became insolvent.

NOTE

Subsections (1) and (2) have the effect that an assignation is, subject to subsection (8), ineffective as regards a claim if the assignor is insolvent at the time of becoming the holder of the claim.

Example A tradesman assigns future invoices to a factor. The tradesman is sequestrated, and then issues an invoice for a new job carried out after the date of sequestration. The claim in respect of that invoice will not transfer to the factor.

Subsection (8) has the effect that an assignation is effective where the claim is in respect of income from property in existence at the time the assignor becomes insolvent, and that is not attributable to anything agreed to be done (or done by) the assignor after the insolvency.

Example 1 A musician has licensed the use of a song in an advert, and assigns the royalties due in respect of that use. The assignation is effective on an insolvency.

Example 2 A landlord assigns the future rent on a property to a bank. The landlord is sequestrated. The assignation remains effective for rents arising after the date of

sequestration because the rents derive from an asset (the property) of, and not from efforts by, the landlord.

Subsection (4) provides for the meaning of insolvency for that purpose, in respect of both individuals and legal persons (such as limited companies).

An assignation that is ineffective under subsection (2) does not become effective if the debtor is discharged from the insolvency.

However, claims that remain effective on an insolvency may become ineffective under subsections (5) and (6) if the debtor is discharged from a sequestration or from a protected trust deed. The effect is that any claim which comes into being after such a discharge is not transferred by the assignation, with the effect that the debtor is helped to make a fresh start after insolvency.

Subsections (5) and (6) will mainly benefit individual debtors, as only a few types of legal person can be sequestrated (for example, partnerships). This protection does not otherwise apply to legal persons, and indeed the effect of a corporate insolvency is in nearly all cases the dissolution of the corporation (for example a limited company). See paragraphs 5.10 to 5.112 of the Report.

Subsection (7) gives the Scottish Ministers power to amend the list of insolvency processes in subsection (4), as well as to apply subsections (5) and (6) to circumstances other than sequestration or the granting of a trust deed.

See in general paragraphs 5.105 to 5.109 of the Report.

6 Assignation in part

(1) A claim may be assigned in whole or in part.

(2) But subsection (1) is subject to section 7(2).

(3) And if the claim is not a monetary claim, the claim is only assignable in part where either—

(a) the debtor consents, or

(b) the claim—

(i) is divisible, and

(ii) assigning it in part does not result in the obligation to which it relates becoming significantly more burdensome for the debtor.

(4) Except in so far as the debtor and the assignor otherwise agree, the assignor is liable to the debtor for any expense incurred by the debtor which is attributable to the claim's being assigned in part rather than in whole.

NOTE

Subsection (1) makes it clear that a claim may be assigned in whole or in part. It is based in part on paragraph 5.107 of Chapter 5 of Book III (obligations and corresponding rights) of the DCFR.

Example Andrew lends £2,000 to Brenda. He then has a claim for repayment of that sum. But he could assign £500 of that claim to Carol and the other £1,500 to Doris. These would be assignations in part.

Subsection (2), as read with section 7(2), has the effect that:

- the account debtor (the person who must perform the obligation which is the subject of the claim) and the holder of the claim can agree, or

- the party whose unilateral undertaking gives rise to the claim can stipulate, that assignation in part is not permissible, or is permissible only in particular circumstances.

Subsection (3) provides that where the claim is not one requiring payment of money, then assignation in part is only permissible in two circumstances.

(a) The first is where the debtor consents.

(b) The second is where the claim is divisible, and the assignation in part does not result in a significantly greater burden on the debtor.

Thus say Elaine has an obligation to deliver 30 motor vehicles to Frank. Her obligation may not become significantly more burdensome if Frank assigns part of his claim to one person and the remainder to another. If however Frank assigns the claim to 30 persons then the obligation may well become significantly more burdensome (and therefore not assignable in part in that manner).

Subsection (4) enables the debtor to recover from the assignor, unless agreed otherwise, the expenses attributable to a claim being assigned in part under subsection (1).

Example Sending payments to several partial assignees rather than one assignee may be more costly.

This section does not make provision as to how any consent or agreement for the purposes of this section is to be constituted. It might, for example, be in the agreement which gives rise to the claim or in a subsequent agreement.

See in general paragraphs 4.31 to 4.34 of the Report.

7 Limitations as to assignability

(1) Section 1 is subject to any other enactment, or any rule of law, by virtue of which the assignation of a claim is of no effect.

(2) The assignation of a claim is of no effect if and in so far as—

(a) the debtor and the holder of the claim had agreed, or

(b) the person whose unilateral undertaking gives rise to the claim had stated,

that the claim was not to be assigned.

(3) In subsection (2)(a), "holder of the claim" includes, without prejudice to the generality of that expression, a person who did not become holder of the claim until after the agreement had been made.

(4) Subsection (2) is subject to any other enactment.

NOTE

Subsection (1) continues the effect of any current enactment or rule of law that prevents the assignation of a claim. For example, the assignation of a claim to certain social security payments is barred by section 187 of the Social Security Administration Act 1992.

Subsection (2) makes it clear that the debtor and the holder of the claim can agree, or a person giving a unilateral undertaking can state, that the claim cannot be assigned whether in whole or in part. This is known as an anti-assignation (or following England and Wales, a non-assignment) clause.

Subsection (3) confirms that the holder of the claim, for the purposes of an agreement under subsection (2), can include a person who is not yet the holder at the time of agreement.

Subsection (4) has the effect that subsection (2) is subject to any enactment which renders anti-assignation clauses ineffective, such as sections 1 and 2 of the Small Business, Enterprise and Employment Act 2015.

As for section 6, this section does not make express provision as to how any agreement or statement is to be constituted.

See paragraphs 13.2 to 13.11 of the Report.

8 Claim in respect of wages or salary

(1) It is not competent for an individual to assign a claim in respect of wages or salary payable to the individual.

(2) For the purposes of subsection (1), "wages" and "salary" are, without prejudice to the generality of those expressions, to be taken to include—

(a) any—

(i) fee,

(ii) bonus,

(iii) commission,

(iv) holiday pay, or

(v) other emolument,

referable to the individual's employment (whether or not payable under the individual's contract of employment),

(b) any payment in respect of expenses incurred by the individual in carrying out that employment, and

(c) if the individual is dismissed from that employment by reason of redundancy, any payment referable to the redundancy.

(3) Subsection (1) is without prejudice to any other enactment.

NOTE

This section prevents an individual assigning a claim to payments of wages or salary due to him or her, including for that purpose any associated payments such as bonus and redundancy payments. It clarifies that existing statutory provisions preventing assignation of wages etc. in particular cases will continue to have effect.

See paragraphs 5.101 to 5.104 of the Report.

9 Intimation of the assignation of a claim

(1) For the purposes of section 3(2)(b)(i), intimation is effected (and is effected only)—

(a) by there being served on the debtor, by the assignor or the assignee, notice of the assignation, or

(b) on the occurrence either—

(i) of the debtor acknowledging to the assignee that the claim is assigned, or

(ii) of intimation to the debtor, in judicial proceedings to which the debtor is a party, that the assignation is founded on in the proceedings.

(2) Where in respect of any claim there are co-debtors, intimation so effected as respects any one or more of them is, for the purposes of section 3(2)(b)(i), intimation to them all.

(3) A notice served under subsection (1)(a)—

(a) must—

(i) set out the name and address both of the assignor and of the assignee and provide details of the claim assigned and, in the case of a claim assigned in part, details also of the part assigned, or

(ii) provide (but only if the notice is served as mentioned in subsection (4)(c)) an electronic link to a website, or to a portal, in which the information mentioned in sub-paragraph (i) is set out,

(b) need not be executed or authenticated,

(c) if the claim is a monetary claim, may (but need not) be in a form prescribed for the purposes of this paragraph, and

(d) must consist of, or be contained within, a document (but that document need not be a single document).

(4) For the purposes of subsection (1)(a), service of a notice must be by—

(a) delivering the notice personally to the debtor,

(b) sending it—

(i) by postal services, or

(ii) by any other service which conveys postal packets from one place to another,

either to the proper address of the debtor or to an address for postal communication provided to the assignor by the debtor, or

(c) transmitting it to an address for electronic communication so provided.

(5) Without prejudice to the generality of subsection (3)(d), for the purposes of that subsection "document" includes—

(a) an e-mail, and

(b) an attachment to an e-mail.

(6) In subsection (4)(b), "postal packet" and "postal services" have the meanings given to those expressions by section 27(1) and (2) of the Postal Services Act 2011.

(7) For the purposes of subsection (4)(b), the "proper address" of the debtor is—

(a) in the case of a body corporate, the address of the registered or principal office of the body,

(b) in the case of a partnership, the address of the principal office of the partnership, and

(c) in any other case, the last known address of the debtor.

(8) Where a notice is served—

(a) as mentioned in subsection (4)(b), or

(b) where there has been a determination under subsection (11)(b), as mentioned in that subsection as it applies by virtue of the determination,

by being sent to an address in the United Kingdom, it is to be taken to have been received 48 hours after it is sent unless it is shown to have been received earlier.

(9) Where a notice is served as mentioned in subsection (4)(c), it is to be taken to have been received 24 hours after it is transmitted unless it is shown to have been received earlier.

(10) A determination such as is mentioned in subsection (11) may be made—

(a) by written agreement between the debtor and the holder of the claim, or

(b) where a unilateral undertaking gives rise to the claim, by written statement (whether or not comprised within the undertaking) of the person whose undertaking it was.

(11) The determination is (either or both)—

(a) that only certain of the paragraphs and sub-paragraphs of subsection (4) (being paragraphs and sub-paragraphs specified in the determination) are, for the purposes of section 3(2)(b)(i), to apply as respects the claim,

(b) that, as respects the claim, subsection (4)(b) is to apply as if, for the reference to sending a notice "either to the proper address of the debtor or to an address for postal communication provided to the assignor by the debtor" there were substituted a reference to sending it to a particular address (being an address specified in the determination).

(12) In subsection (10)(a), "holder of the claim" includes, without prejudice to the generality of that expression, a person who did not become holder of the claim until after the agreement had been made.

(13) Any reference in the preceding provisions of this section to—

(a) a notice being served on the debtor, is to be construed as including a reference to its being served on a person authorised to receive such a notice on behalf of the debtor,

(b) the proper address of the debtor, is to be construed as including a reference to the proper address of a person so authorised.

NOTE

Section 3 of the Bill sets out that an assigned claim may be transferred by intimation under subsection (1) of this section.

Subsection (1) therefore sets out a new rule on the types of intimation that must be used in order to effect the transfer of a claim. It replaces the existing statutory rules on intimation in the Transmission of Moveable Property (Scotland) Act 1862, which is therefore repealed by section 41 of the Bill.

Subsection (1)(a) provides that either the assignee or the assignor may serve notice of the assignation on the debtor. The effect when read with subsections (3) and (5) is that written notice is required, although it may be in electronic form.

Subsection (1)(b) provides, first, for "constructive" intimation to a debtor who has knowledge of the assignation of the claim.

> Example — Having become aware of the assignation other than by notice, the debtor may perform – or promise to perform - to the assignee something which the assigned claim obliges the debtor to perform. The claim is transferred by the performance or the promise without any need for written intimation to the debtor.

Subsection (1)(b) provides, second, for intimation to be given, and the claim transferred, where the debtor is a party to judicial proceedings in which the assignation is founded on.

> Example — The assignee raises an action against the debtor for performance of the obligation to which the claim relates. Thus if Andrew lends £2,000 to Brenda, and then he assigns the right to repayment to Carol, intimation to Brenda would be effected by Carol raising proceedings against her founding on the assignation.

Subsection (2) confirms that intimation to any one co-debtor is to be treated as intimation to all the co-debtors, as under the existing law.

> Example — Kenneth lends £1,000 to Leslie and Max. If he assigns the right to repayment to Nicola then the claim will be transferred to her by intimation to either Leslie or Max.

Subsections (3) to (12) provide more detail on assignation by notice to the debtor.

Subsection (3) concerns the form and content of the notice. It should be read with section 15 of the Bill which sets out the right of the debtor to seek information about an assignation. The notice must provide (i) the name and address of both the assignor and assignee; and (ii) details of the claim (or part claim) being assigned. In the case of an electronic intimation the required information may be provided through a link to a website or portal.

A notice under subsection (3) need not be signed (in ink or electronically) and need not be set out in a single document. The effect is to authorise the practice of some factors whereby stickers are placed on invoices instructing the debtor to pay the factor, but the stickers are not signed.

Subsection (3) also provides for a power for the Scottish Ministers to prescribe a style form of notice for the assignation of monetary claims. While the style would not be mandatory, it could be helpful to parties involved in assignations to have a clear statutory style.

Subsections (4) to (11) provide for service of the notice, and are based on section 26 of the Interpretation and Legislative Reform (Scotland) Act 2010.

Subsection (4) permits three forms of service: (a) by personal delivery; (b) by post or courier; and (c) by electronic transmission. The Bill deviates from section 26 of the 2010 Act by allowing ordinary post and couriering because modern debt-factoring practice is to use this rather than registered delivery (despite it being harder to prove delivery). Intimation can be made either to the "proper address" of the debtor as defined in subsection (7), or an address supplied by the debtor.

Subsection (5) makes it clear that "document", for the purposes of a notice under subsection (3), includes an email or an attachment to an email.

Subsection (6) defines certain terms by reference to the Postal Services Act 2011.

Subsection (8) provides that a notice served by post or other postal services in the UK is deemed to be received 48 hours later unless earlier receipt can be shown. Subsection (9) sets out a similar rule for electronic transmission, in that case it is deemed to be received after 24 hours.

The effect is to provide, where required, certainty as to the time of intimation. This is important in a question with third parties, such as creditors carrying out diligence, as the claim will transfer on intimation.

If the notice has not actually reached the debtor (for example, by going missing in the post) then the good faith protection rule in section 11 applies.

Subsections (10) and (11) allow the parties to make a determination that a notice must be served by means of one of the permitted ways (e.g. by electronic means), or to a particular address. In other words, the default rules can be replaced up to a point. Intimation by oral means is not however permitted.

Subsection (12) makes it clear that a determination can be entered into between a debtor and the prospective holder of a claim.

Subsection (13) allows service to be made on a party who is authorised to act on behalf of the debtor for that purpose, such as a solicitor.

See in general paragraphs 5.34 to 5.72 of the Report.

10 Warrandice implied in the assignation of a claim

(1) Subsections (2) to (4) apply except in so far as the assignor and the assignee otherwise agree.

(2) In assigning a claim—

(a) for value, the assignor is taken to warrant to the assignee that—

(i) the assignor is entitled to, or (in the case of any such claim as is mentioned in section 1(5)) will be entitled to, transfer the claim to the assignee,

(ii) the debtor is obliged to, or (when performance becomes due) will be obliged to, perform in full to the assignor, and

(iii) the assignor has done nothing, and will do nothing, to prejudice the assignation,

(b) other than for value, the assignor is taken to warrant to the assignee that the assignor will do nothing to prejudice the assignation.

(3) In assigning a claim, whether for value or other than for value, the assignor is not taken to warrant to the assignee that the debtor will perform to the assignee.

(4) Subsections (2) and (3) apply in relation to providing, in a contract or unilateral undertaking, for the assignation of a claim as they apply in relation to assigning a claim.

NOTE

This section provides for the warranties that an assignor is deemed, unless agreed otherwise, to give to the assignee in respect of an assigned claim. It replaces the current law, and clarifies the effect of warrandice. See section 17(1)(d) for the repeal of the current law.

Subsection (2) provides for both assignations for value and for gratuitous (for no value) assignations. In the first case the implied warrandice reflects the common law principle of warrandice *debitum subesse* (the

debt exists). In the second case the implied warrandice reflects the common law principle of warrandice of facts and deeds only.

Subsection (3) makes it clear that the assignee is not held to warrant that the debt will be paid. In other words, the assignor does not guarantee that the debtor is solvent and can pay the debt.

Subsection (4) has the effect that the warranties are, where applicable, implied in any contract relating to the assignation of a claim as well as in the assignation itself.

See paragraphs 13.36 to 13.43 of the Report.

Protection of debtors

11 Protection of debtor who performs in good faith

(1) Subsection (2) applies where, after a claim is transferred, the debtor, or any co-debtor, performs to the person last known to the debtor, or that co-debtor, to be the holder of the claim.

(2) If the performance is in good faith, the debtor is discharged from the claim to the extent of the performance.

(3) It is not to be taken, by reason only of (any or all of)—

(a) an assignation document's having been registered,

(b) the application of section 9(8),

(c) the application of section 9(9),

that for the purposes of subsections (1) and (2) a debtor, or any co-debtor, has performed other than in good faith.

NOTE

Under the existing law, a claim will only transfer if it is intimated to the debtor, but the effect of the changes in the Bill is both to extend the scope of intimation and to enable registration as a method of effecting a transfer of a claim.

The debtor may not know that a claim has been assigned, and may therefore in good faith pay an assignor who is no longer the creditor. This section has the effect that a debtor who does not, and should not, know that a claim has been assigned will still be discharged from the debt to the extent of any payment made to the assignor (or any person nominated by the assignor).

Example Paul lends Roger £5,000. Paul assigns his right to repayment to Susan, and she registers the assignation in the RoA. The effect is to transfer the claim so that payment is due to Susan. But Roger who knows nothing of the assignation repays Paul, who accepts payment rather than telling Roger to pay Susan. Roger does not require to pay Susan any amount that he has paid in good faith to Paul.

Subsections (1) and (2) provide for a general rule protecting a debtor who performs in good faith to the assignor where a claim has been assigned in whole or in part.

The "last known holder of the claim" formulation in subsection (1) deals with the fact that there may have been a chain of assignations rather than only one.

Subsection (3) provides that the fact that an assignation has been registered, or that it is deemed to have been intimated, does not of itself mean that the debtor does not perform in good faith. In particular, debtors should not be expected to have to check the RoA.

Good faith is not further defined in this section. But see section 120 which places the onus of showing that the debtor has performed other than in good faith on the person making such an assertion. The concept is to an extent subjective, and whether or not a debtor is in good faith will depend on the facts of the case.

Example — Susan might make intimation to Roger by means of sending him a 200-page document dealing with many matters, but including the words of intimation half way down page 172. Roger may be in good faith if he still pays Paul.

See paragraphs 12.2 to 12.9 of the Report.

12 Further provision as to protection of debtor

(1) Subsection (2) applies where—

(a) the holder of a claim purports to assign the claim (or one and the same part of the claim) by means of more than one assignation document, each in favour of a different person,

(b) the claim (or part) is transferred as mentioned in section 3(1), or by virtue of section 4(2)(a), to one of those persons,

(c) the debtor, or any co-debtor, receives notice from the other of those persons (or as the case may be from another of those persons), ostensibly by virtue of section 9(1)(a) or (b)(ii), of the purported assignation to that other person, and

(d) by virtue of such notice the debtor, or any co-debtor, performs to that other person.

(2) If the performance is in good faith, the debtor is discharged from the claim (or part) to the extent of the performance.

(3) Subsection (3) of section 11 applies for the purposes of subsections (1) and (2) as it applies for the purposes of subsections (1) and (2) of that section.

NOTE

This section provides protection for debtors who are in good faith where an assignor is not.

Subsection (1) sets out the four criteria which must each be met in order for the protection in subsection (2) to apply:

(a) The first criterion is that the holder of the claim grants more than one assignation document in respect of the same claim (or part claim),

(b) The second criterion is that the claim is transferred by one of the assignations to the true holder (typically, by registration of the assignation),

(c) The third criterion is that the assignee in another of the assignations informs the debtor, either by notice or by being made party to judicial proceedings, that the claim is assigned to that assignee (the purported holder), and

(d) The fourth criterion is that by virtue of being so informed the debtor performs to the purported holder.

Subsection (2) has the effect that if the performance to the purported holder is in good faith then the debtor is discharged from the claim (or part) to that extent, and does not need to compensate the true holder.

Example Liana lends Kimberley £1,000, who then assigns her claim to Monica. Monica registers the assignation in the Register of Assignations (and does not intimate). Kimberley then assigns the same claim again to Neil, who does intimates to Liana. Liana pays Neil, who is not the true holder, but provided she is in good faith she is discharged from the obligation to pay Monica.

Subsection (3) imports the rules that apply under section 11 of the Bill, namely that the debtor is not in bad faith merely because an assignation has been registered in the RoA, or because intimation has been deemed to have taken place.

See also section 120 of the Bill which places the onus of showing that the debtor has performed other than in good faith on the person making such an assertion.

See paragraphs 12.10 to 12.12 of the Report.

13 Performance in good faith where claim assigned is of a prescribed type

(1) Subsection (2) applies where—

(a) by virtue only of being of a type prescribed under section 3(6), a claim assigned is not transferred, and

(b) the debtor, or any co-debtor, performs in good faith to the assignee.

(2) The debtor is discharged from the claim to the extent of the performance.

(3) For the purposes of subsection (1)(b) a debtor, or co-debtor, who knows—

(a) that the assignation document has not been registered, and

(b) that transfer of the claim requires such registration,

is not to be taken to perform in good faith.

NOTE

This section protects debtors who in good faith pay the assignee in an assignation that should have been registered (see section 3(6) of the Bill) but was not.

Subsection (1) sets out the two criteria which must each be met in order for the protection in subsection (2) to apply:

(a) The first criterion is that the assignation relates to a claim of a type prescribed by the Scottish Ministers under section 3(6) of the Bill as being a claim that can only be transferred by registration, and the assignation has not been registered,

(b) The second criterion is that, despite the claim not having transferred, the debtor performs in good faith to the assignee (perhaps because the assignation has been intimated).

Subsection (2) provides that the debtor is discharged from the claim (or part) to the extent of the performance to the assignee.

Subsection (3) sets out that the debtor will not be in good faith if the debtor knows that the assignation has not been registered, and that registration was required in order to transfer the claim, and still pays the purported assignee (who is not the holder).

See paragraphs 12.13 to 12.15 of the Report.

14 Asserting defence or right of compensation

(1) Except in so far as the debtor and the assignor otherwise agree, the debtor, or any co-debtor, may assert against the assignee—

(a) any defence which the debtor has the right to assert against the assignor,

(b) any right of compensation which, immediately before the time mentioned in subsection (2), was available to the debtor against the assignor.

(2) That time is the time at which the debtor would no longer have been in good faith had the debtor performed to the assignor.

(3) Subsection (3) of section 11 applies for the purposes of subsections (1) and (2) as it applies for the purposes of subsections (1) and (2) of that section.

(4) In so far as it allows for an exception, subsection (1) is without prejudice to any other enactment.

(5) Without prejudice to the generality of subsection (1)(b), for the purposes of this section a right of compensation includes a right of contractual set-off but only if the basis of the right included is the contract which gives rise to the claim assigned.

NOTE

This section puts the common law rule *assignatus utitur jure auctoris* (the assignee takes the rights of the assignor) into statutory form. It is also based in part on paragraph 5.116 of Chapter 5 of Book III (obligations and corresponding rights) of the DCFR.

The new rule applies by default, so that it is open to the debtor and the assignor to agree that the debtor may not assert a particular right. This section does not make express provision as to how any agreement is to be constituted, although it will need to pre-date the assignation. See paragraphs 12.35 to 12.38 of the Report.

The effect of subsection (1)(a) is that, unless agreed otherwise, any defences which the debtor can plead against the assignor can also be pled against the assignee.

Example — Ona sells goods to Peter at a price of £1,000. The sale is on credit, and Ona assigns her claim for payment to Quentin. It turns out that the goods are defective. If this entitled Peter to refuse to pay Ona then he is equally entitled to refuse to pay Quentin. It does not matter that Quentin is in good faith.

Subsections (1)(b) and (5) provide a special rule for compensation (which includes contractual set-off).

Example — Ian owes John £1,000, but John owes Ian £200. Ian is entitled to set-off the £200 debt and only pay John £800. This right to set-off remains valid if John assigns his claim to £1,000 to Kirsten. Ian only has to pay Kirsten £800.

Subsection (2) has the effect that compensation can be pled in respect of any debt becoming due in the period up to the date that the debtor knows that there has been an assignation. This replaces the existing

law that compensation can only be pled in relation to debts which arose prior to the date of intimation of the assignation, and is necessary because under the Bill a claim can transfer by registration.

Subsection (3) applies the rules set out in section 11(3) here too. See the commentary to that provision.

Subsection (4) states that any agreement made by the parties that a defence cannot be asserted against the assignee is subject to a contrary rule in any enactment. For example, a consumer debtor may be protected by the unfair contract terms provisions in the Consumer Rights Act 2015.

See in general paragraphs 12.27 to 12.34 of the Report.

15 Right to withhold performance until evidence of, or statement as to, assignation is provided

(1) A debtor on whom a notice of assignation of a claim is served under section 9(1)(a) by an assignee may request from the assignee sufficient evidence of the assignation.

(2) Without prejudice to the generality of subsection (1), for the purposes of that subsection "sufficient evidence" may be the written confirmation of an assignor that an assignation to which that assignor is party has taken place.

(3) A debtor who, other than by virtue of section 9(1)(a), has reasonable grounds to believe that a claim has been assigned, may state those grounds to the supposed assignor and request that person to provide a written statement as to whether the claim has been assigned.

(4) If a written statement provided by virtue of subsection (3) is to the effect that the claim has been assigned, that statement must include the name and address of the assignee.

(5) If—

(a) evidence is requested under subsection (1), the debtor may withhold performance until—

(i) that evidence is received, or

(ii) (whether or not in response to a request under subsection (3)) the debtor receives from the supposed assignor a written statement that the claim has not been assigned, or

(b) a written statement is requested under subsection (3), the debtor may withhold performance until that statement (conforming, where it is a statement to the effect mentioned in subsection (4), with the requirements of that subsection) is received.

NOTE

This section provides protections for debtors who might otherwise pay a purported assignee of a claim rather than the true holder of the claim.

It will often be the case that the debtor has little or no knowledge of an assignee, either before or after an assignation is intimated (given that there is no requirement to include a copy of the assignation document when intimating the assignation).

Subsection (1) applies where notice of an assignation has been given to the debtor, and has the effect that the debtor may request sufficient evidence of the assignation from the assignee.

Example George owes Henry £500. Henry assigns the claim for payment to Imogen, who registers the assignation in the RoA, and then assigns to Jay who intimates to George. George can request sufficient evidence of the Imogen/Jay assignation.

Subsection (2) gives an example of "sufficient evidence", namely written confirmation of the assignation from the assignor. There is no express requirement to provide a copy of the assignation document as it may contain information confidential to the assignor/assignee or a third party.

Subsections (3) and (4) apply where the debtor has not received a formal notice of the assignation, but has reasonable grounds to believe that the claim has been assigned. The debtor may state those grounds to the supposed assignor, and require that party to confirm the position in writing. If the claim has been assigned then the assignor must provide the name and address of the assignee.

A request for evidence, or a statement of grounds, need not be in writing.

Subsection (5) sets out the remedy where no reply is received to an enquiry in either of the above cases. The debtor is entitled to withhold performance from each of the assignor and the assignee until the evidence or a statement is provided.

Subsection (5)(a)(ii) prevents performance being withheld where the assignor confirms that there has been no assignation. This deals with the situation where the "assignee" is a fraudster who wants to prejudice the holder of the claim by making a fake intimation.

The right to withhold performance under this section is a free-standing right and separate from the protections provided for by sections 11 to 13 of the Bill.

See paragraphs 12.17 to 12.26 of the Report.

Accessory security rights

16 Accessory security rights

(1) Subsections (2) and (3)—

(a) apply in relation to any claim assigned in whole, and

(b) do not apply in relation to any claim assigned in part,

but are subject to any express provision to the contrary in the assignation document.

(2) Without prejudice to subsection (3), the assignee acquires, by virtue of the assignation, any security (in so far as the security is transferable) which relates to, and only to, the claim assigned.

(3) Where the performance of some act by the assignor is requisite for the transfer of the security to the assignee, the assignor must as soon as reasonably practicable perform that act.

(4) In this section, "security" means both—

(a) a right in security, and

(b) the correlative right in respect of a cautionary obligation.

NOTE

It is an existing rule of Scots law that where a claim is assigned the assignee is entitled to the benefit of any accessory rights enjoyed by the assignor. This section puts the rule onto a statutory footing as regards accessory security rights.

Subsection (1) provides for this section to apply to a claim assigned in whole. It makes it clear that the rule in subsection (2) is a default rule, leaving it open to the parties to an assignation to agree that a right will not be acquired.

If only part of the claim is assigned then it is less clear whether, and to what extent, the assignee should acquire an accessory right. Any such right may for example relate to the whole obligation, and it is expected that the parties will make their own provision in such cases. If they do not then the partial assignation will not carry the security right.

Subsection (2) has the effect that the assignation will transfer any security which relates to the claim assigned, and is restricted to that claim.

Example 1	David lends Edgar £100,000. Edgar grants a standard security over his house in respect of the £100,000 debt. If David assigns the right to repayment of the £100,000 to Flora then she acquires the security unless agreed otherwise.
Example 2	As for example 1, but the standard security is granted for all sums due and that may become due. The assignation of the right to repayment of the £100,000 does not carry the security unless agreed otherwise, because the security is not restricted to the £100,000.
Example 3	Same as for example 2, but the assignation document expressly states that the all sums security is carried. Flora acquires the security.

In terms of subsection (3), if the assignee acquires a security under this section then the assignor is required as soon as reasonably practicable to perform any steps necessary to transfer the security. For example, in the case of a standard security, an assignation under section 14 of the Conveyancing and Feudal Reform (Scotland) Act 1970 would require to be registered in the Land Register of Scotland to be effective.

Subsection (4) defines "security" as including both a right in security (see section 42(3) of the Bill) and cautionary obligations (such as a personal security or guarantee).

See paragraphs 13.26 to 13.33 of the Report.

Abolition of certain rules of law

17 Abolition of certain rules of law

(1) The following rules of law are abolished—

(a) any rule whereby a mandate may operate as an assignation of a claim,

(b) any rule whereby an assignation is rendered ineffective by an instruction to the debtor by an assignee of a claim that the debtor perform to the assignor,

(c) any rule whereby an assignee of a claim may sue in the name of an assignor, and

(d) any rule as to warrandice to be implied—

(i) in assigning a claim, or

(ii) in providing, in a contract or unilateral undertaking, for the assignation of a claim.

(2) But subsection (1)(c) is without prejudice to the application of any—

(a) enactment, or

(b) rule of law,

as respects subrogation.

NOTE

Subsection (1) abolishes four common law rules.

The first is any rule that a mandate (personal instruction) to deal with a claim may operate as an assignation of the claim. The existing law is unclear, and abolishing any such rule will therefore clarify the law. See paragraphs 13.14 to 13.20 of the Report.

The second is any rule under which an assignation is made ineffective by an instruction to the debtor by the assignee to continue to perform to the assignor. There is some authority suggestive of such a rule, which is inconvenient in commercial practice. See paragraphs 5.58 to 5.61 of the Report.

The third rule is the one permitting the assignee to sue in the name of the assignor. The effect is that the assignee must raise proceedings in his or her own name. Again, see paragraphs 13.14 to 13.20 of the Report.

The fourth rule is any rule in relation to the warrandice to be implied in an assignation, or a contract relating to an assignation. Section 10 now deals with this matter, and see also paragraph 13.43 of the Report.

Subsection (2) makes it clear that the abolition of the third rule described above is without prejudice to any rule as respects subrogation, which may be regarded as a form of assignation. The effect is to preserve the well-established practice that insurers sue in the name of the insured in personal injury and other insurance cases. Again, see paragraphs 13.14 to 13.20 of the Report.

Saving

18 Saving as respects International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015

(1) This Part is without prejudice to the application, as respects the assignment and acquisition of associated rights, of the International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015 (S.I. 2015/912).

(2) In subsection (1)—

"assignment" has the meaning given to that expression by regulation 5, as read with regulation 35, of those regulations, and

"associated rights" has the meaning given to that expression by regulation 5 of those regulations.

NOTE

This is a saving provision which relates to certain rights (known as "associated rights") which are governed by the 2015 Regulations (S.I. 2015/912).

The 2015 Regulations implement the 2001 Convention on International Interests in Mobile Equipment (the "Cape Town Convention"). The Convention was agreed under the auspices of the International Institute for the Unification of Private Law, also known as UNIDROIT.

The Cape Town Convention makes provision, amongst other things, for an international security right in respect of aircraft objects as defined in the Convention. There are special rules in relation to the assignment (assignation) of such a right, and the effect of this section is that these rules take precedence over the provisions in Part 1 of the Bill.

For example, regulation 27 of the 2015 Regulations deals with the effect of the assignment of "associated rights" (rights to payment or to other performance) on the related international interest.

See paragraph 13.46 of the Report.

CHAPTER 2

REGISTER OF ASSIGNATIONS

Register of Assignations

19 The Register of Assignations

(1) There is to be a public register known as the Register of Assignations.

(2) The Register of Assignations (in this Part referred to as "the register") is to be under the management and control of the Keeper.

(3) Subject to the provisions of this Act the register is to be in such form as the Keeper thinks fit.

(4) The Keeper is to take such steps as appear reasonable to the Keeper for protecting the register from—

(a) interference,

(b) unauthorised access, or

(c) damage.

(5) Section 110 of the Land Registration etc. (Scotland) Act 2012 (fees) applies in relation to the register as it applies in relation to any other register under the management and control of the Keeper.

NOTE

Subsection (1) establishes a new register for the registration of assignations of claims. The register is to be known as the "Register of Assignations" ("RoA"). See paragraphs 6.2 to 6.7 of the Report.

Subsection (2) provides that the register is to be under the management of the Keeper of the Registers of Scotland (see section 118(1) of the Bill for the definition of "Keeper"). See paragraphs 6.8 to 6.10 of the Report.

Subsection (3) states that, subject to the requirements laid down by the Bill, the Keeper has discretion as to the form in which the register is kept. See paragraphs 6.31 to 6.32 of the Report. That will therefore include the RoA being kept in a wholly electronic form.

The RoA, as with the other registers under the Keeper's control, is an important public asset. Subsection (4) therefore provides that the Keeper is to take such steps as appear reasonable to protect the RoA from interference, unauthorised access or damage (for example by hacking).

Subsection (5) enables the Scottish Ministers, in consultation with the Keeper, to set fees in relation to the RoA using their powers in section 110 of the Land Registration etc. (Scotland) Act 2012. See paragraph 6.11 of the Report.

See also section 40 of the Bill, which provides for the Scottish Ministers by regulations to make rules ("RoA Rules") as to the keeping of the RoA and related matters.

Structure

20 The parts of the Register of Assignations

The Keeper must make up and maintain, as parts of the register—

(a) the assignations record, and

(b) the archive record.

NOTE

See paragraph 7.2 of the Report.

21 The assignations record of the Register of Assignations

(1) An entry in the assignations record is to include—

(a) the assignor's name and address,

(b) where the assignor is an individual, the assignor's date of birth,

(c) any number which the assignor bears and which, by virtue of RoA Rules, must be included in the entry,

(d) the assignee's name and address,

(e) any number which the assignee bears and which, by virtue of RoA Rules, must be included in the entry,

(f) where the assignee is not an individual, an address (which may be an e-mail address) to which any request for information regarding the assignation may be sent,

(g) such description of the claim as may be—

(i) required, or

(ii) permitted,

for the purposes of this subsection by RoA Rules,

(h) a copy of the assignation document,

(i) the registration number allocated under section 23(4)(b) to the entry,

(j) the date, and time of registration, of the assignation document, and

(k) such other data as may be required by virtue of any other section of this Act (including, without prejudice to the generality of this paragraph, such other data as may be specified for the purposes of this subsection by RoA Rules).

(2) The assignations record is the totality of all such entries.

NOTE

This section sets out the information which must be included in an entry in the assignations record, and provides that the assignations record is the totality of such entries.

The details of the assignee will be included in the entry in the assignations record, but a search against the assignee under section 32 of the Bill is not permitted (unless the Scottish Ministers specify in RoA Rules made under section 40 of the Bill that such a search is permitted). It will however be possible for an entitled person as defined in section 36 of the Bill to request information under that section about the assignation from the assignee.

An assignor or assignee may be a legal person with a unique identifying number, such as a UK limited company or limited liability partnership. The Scottish Ministers will be able to specify that these unique numbers are included in the entry in the assignations record: see section 40(1)(c)(ii) of the Bill.

This section provides that an entry in the assignations record must include a copy of the assignation document. The Scottish Ministers may however specify that information in the record, including information in the assignation document, will not be disclosed in a search of the RoA in order to protect confidential information of the parties.

See paragraphs 7.3 to 7.27, and 7.41, of the Report.

22 The archive record of the Register of Assignations

The archive record—

(a) is the totality of all entries and copy documents transferred from the assignations record under section 28(4)(a) or (b) or 29, and

(b) includes such other data as may be specified for the purposes of this section by RoA Rules.

NOTE

This section sets out that the archive record is the totality, first, of the entries which have been transferred to that record from the assignations record and, second, of any other data required to be entered in the record by RoA Rules.

See paragraphs 11.19 to 11.21 of the Report.

Applications for registration

23 Application for registration of assignation document

(1) An application for registration of an assignation document may be made to the Keeper by the assignee.

(2) The Keeper must accept the application if—

(a) it—

(i) conforms to such RoA Rules as may relate to the application, and

(ii) is submitted with a copy of the assignation document,

(b) the Keeper has such data as the Keeper requires, by virtue of section 21(1), to make up an entry for the assignation document, and

(c) either—

(i) such fee as is payable for the registration is paid, or

(ii) arrangements satisfactory to the Keeper are made for payment of that fee.

(3) If the requirements of any of paragraphs (a) to (c) of subsection (2) are not satisfied, the Keeper must reject the application and inform the applicant accordingly.

(4) On accepting an application made under subsection (1), the Keeper—

(a) must—

(i) make up an entry for the assignation document (from that document, the data provided in the application and the circumstances of registration), and

(ii) maintain the entry in the assignations record, and

(b) must allocate a registration number to the entry.

NOTE

Subsection (1) enables the assignee, and only the assignee (or the assignee's agent – see 118(4)), to apply to the Keeper to register an assignation in the Register of Assignations. See paragraphs 6.21 to 6.30 of the Report.

Subsection (2) sets out that the Keeper must accept the application if it is in due form as specified in this section, conforms to RoA Rules, and the fee due to the Keeper is - or will be - paid.

Subsection (3) sets out that the Keeper must reject an application that does not conform to subsection (2). See paragraphs 7.28 to 7.30 of the Report.

Subsection (4) provides that the Keeper must on accepting an application make up and maintain the appropriate entry in the RoA, which includes allocating a registration number (as defined in section 118(1) of the Bill).

See in general paragraphs 7.31 to 7.32 of the Report.

Verification statement and date and time of registration

24 Verification statement as to registration of assignation document

(1) The Keeper must after the registration, by virtue of an application made under section 23, of an assignation document, issue to the assignee a written statement verifying the registration.

(2) That statement must—

(a) conform to such RoA Rules as may relate to the statement, and

(b) include—

(i) the date and time of the registration, and

(ii) the registration number allocated to the entry made up for the assignation document.

(3) Where a statement has been issued under subsection (1), the assignor may request from the assignee a copy of that statement.

(4) Within 21 days after a request is made under subsection (3), the assignee must supply the assignor with the copy requested.

NOTE

This section provides that the Keeper must, on accepting an application for registration under section 23 of the Bill, send a statement to the applicant verifying what has been done.

See paragraphs 7.33 to 7.40 of the Report.

25 Date and time of registration of assignation document

(1) An assignation document is taken to be registered on the date and at the time which are entered for that document by virtue of section 21(1)(j).

(2) The Keeper must—

(a) deal with applications for the registration of assignation documents in the order in which they are received, and

(b) allocate registration numbers to the entries to which those applications relate accordingly.

NOTE

Subsection (1) provides that the date and time of registration of an assignation will be the date and time shown for the relevant registration in the assignations record (for which see section 21(1)(j) of the Bill).

Subsection (2) requires the Keeper to process applications for registration of assignations in the order in which they are received, and number them accordingly. The effect is to protect the priority of registration of an assignation (and therefore of ranking of claims in for example an insolvency).

Effective registration

26 Effective registration of assignation document

(1) The registration of an assignation document is ineffective if—

(a) the entry made up for the assignation document in the assignations record does not include a copy of that document,

(b) the data included, by virtue of section 21(1), in that entry contains an inaccuracy which, as at the time of registration, is seriously misleading, or

(c) the assignation document is invalid.

(2) But subsection (1) is subject to section 27(8) to (10).

(3) A registration ineffective by virtue of subsection (1) becomes effective if and when the entry is corrected.

NOTE

Subsections (1) and (2) set out three cases in which a purported registration in the assignations record is ineffective, with the result that the claim will not transfer by reason of registration.

The first case is that the entry does not include a copy of the assignation document.

The second case is that the entry contains an inaccuracy which, as at the time of registration is "seriously misleading" (for which see section 27(1)).

The third case is that the assignation document is invalid, for example because it is a forgery.

Subsection (2) qualifies subsection (1), with the effect that a registration may be either wholly or partly effective.

Subsection (3) enables an ineffective registration to become effective by means of a correction. The effect of this provision, when read with section 31(2) of the Bill, is that the registration becomes effective on the date of the correction. See paragraphs 9.33 to 9.34 of the Report.

See in general paragraphs 8.3 to 8.15 of the Report.

27 Seriously misleading inaccuracies in entries in the assignations record

(1) For the purposes of section 26(1)(b), an inaccuracy in an entry in the assignations record is seriously misleading—

(a) if a search of that record in accordance with—

(i) section 32(2)(a)(i) for the assignor's proper name as at the date and time the entry was created, or

(ii) section 32(2)(a)(ii) for the assignor's proper name as at that date and time and the assignor's date of birth,

using the search facility provided under section 33(1)(a), does not disclose the entry, or

(b) where the assignor is a person required by RoA Rules to be identified in that record by a unique number, if a search of that record for that number—

(i) in accordance with section 32(2)(a)(iii), and

(ii) using the search facility provided under section 33(1)(a),

does not disclose the entry.

(2) Subsection (1) is without prejudice to the generality of section 26(1).

(3) Paragraph (a) of subsection (1) is subject to subsection (4).

(4) Where a search mentioned in paragraph (b) of subsection (1)—

(a) discloses an entry, any search mentioned in paragraph (a) of that subsection which does not disclose the entry is to be disregarded,

(b) does not disclose an entry, any search mentioned in paragraph (a) of that subsection which discloses the entry is to be disregarded.

(5) Subsections (1) to (4) apply in relation to a search for—

(a) a co-assignor's proper name as at the date and time the entry in the assignations record is created,

(b) a co-assignor's proper name as at that date and time and a co-assignor's date of birth, or

(c) a unique number by which a co-assignor is identified,

as they apply in relation to the searches mentioned in subsection (1).

(6) Without prejudice to section 26(1), in determining whether an inaccuracy in an entry in the assignations record is seriously misleading no account is to be taken of the assignation document for which the entry was made up.

(7) An inaccuracy in an entry in the assignations record may be seriously misleading irrespective of whether any person has been misled.

(8) Where an inaccuracy in an entry in the assignations record is seriously misleading in respect of only part of the assigned claim, that inaccuracy does not affect the entry in its application to the rest of the claim.

(9) Where—

(a) the assignor consists of two or more co-assignors, and

(b) there is an inaccuracy in an entry in the assignations record, being an inaccuracy which is seriously misleading in respect of a co-assignor but not in respect of both (or all) the co-assignors,

that inaccuracy does not affect the entry in its application to a co-assignor in respect of whom the inaccuracy is not seriously misleading.

(10) Subsection (9) applies in relation to an assignee which consists of two or more co-assignees as it applies in relation to an assignor which consists of two or more co-assignors.

(11) The Scottish Ministers may by regulations amend this section by specifying further instances in which, for the purposes of section 26(1)(b), an inaccuracy in an entry is seriously misleading.

(12) References—

(a) in subsection (1) to "the assignor's proper name", or

(b) in subsection (5) to "a co-assignor's proper name",

are to the person's name in the form determined in accordance with rules under section 40(1)(c)(i).

NOTE

This section makes further provision as to when an entry in the assignations record will contain an inaccuracy which is seriously misleading for the purposes of determining whether a registration is an effective registration for the purposes of section 26 of the Bill.

Section 42(7) of the Bill provides for the meaning of "inaccuracy" in the assignations record.

If a registration contains an inaccuracy that prevents it being disclosed by a properly formatted search, that inaccuracy should generally be regarded as being seriously misleading.

Subsection (1) sets out the circumstances in which an entry will be seriously misleading, and subsection (2) leaves open the possibility that the assignations record will contain other inaccuracies which are seriously misleading.

For example, there may be an inaccuracy in the name or address of an assignee such that an entitled person is unable to make an information request under section 36 of the Bill. Such an inaccuracy is not covered by subsection (1), but might still in the circumstances be seriously misleading, with the effect that the entry would be ineffective (so that the claim does not transfer).

Subsection (1) has the effect that an entry is seriously misleading where a search of the assignations record under section 32 or 33 of the Bill using the criteria specified in this subsection fails to disclose an assignor or a co-assignor. The specified criteria are - as appropriate - the proper name, proper name and date of birth, or unique number.

The proper name of a person is to be determined by RoA Rules, which might also prescribe a hierarchy of document that could be used to evidence a proper name: for example a passport, driving licence, or a birth certificate.

The point at which the search should be able to disclose an entry is the time at which the entry for the assignation was made up in the RoA. This is necessary given that the Bill does not require (as opposed to permit) the updating of an entry to correct a supervening inaccuracy such as a change of name by the assignor, for example on marriage.

Subsections (3) and (4) applies where a search is carried out against the unique number of the assignor (the "first search"). The effect is to ensure that due weight is given to the further certainty provided by a search that includes the unique number.

If the first search discloses the entry then a second search against the name alone (the "second search") that does not disclose the entry is to be disregarded, with the result that the entry is not seriously misleading.

If the first search does not disclose the entry, and the second search does, then the second search is to be disregarded with the result that the entry has an inaccuracy which is seriously misleading.

Subsection (5) applies subsections (1) to (4) to searches against co-assignors.

Subsection (6) provides that in determining whether an inaccuracy is seriously misleading the assignation document is not to be considered (although a copy must still be part of the entry in the assignations record). The effect is that the person searching the record does not have to look at the document to determine whether the details in the record are seriously misleading.

Example An assignation document assigns a claim to the Iron Bank, but the entry in the assignations record shows the assignee as the Silver Bank. The entry is treated as having a seriously misleading inaccuracy even although the true assignee could be discerned from the document.

Subsection (7) makes it clear that whether an inaccuracy is seriously misleading is to be determined objectively, so that an entry may be misleading whether or not any person was actually misled.

Subsections (8) to (10) deal with an inaccuracy that relates to part of a claim, or to one co-assignor. They have the effect that an entry in the assignations record may be seriously misleading in that respect only, and will therefore be partly effective.

Example A single assignation of rents and of other receivables is registered. RoA Rules provide for certain types of claims including rents and receivables to be identified in a tick box on the application form for registration, and for that information to be included in the entry. A failure to tick the rents box would lead to the registration being ineffective as regards the rents, which would not therefore transfer to the assignee. The receivables would however transfer if the relevant box on the application form was ticked.

Subsection (11) enables the Scottish Ministers to make regulations setting out further circumstances in which an inaccuracy is seriously misleading.

Subsection (12) has the effect that a reference in this section to a "proper name" is to a name in the form determined by RoA Rules.

See paragraphs 8.16 to 8.30 of the Report.

Corrections

28 Correction of the assignations record

(1) Subsections (2) and (3) apply where the Keeper becomes aware of a manifest inaccuracy in the assignations record.

(2) The Keeper must correct the record if what is needed to correct it is manifest.

(3) Where what is needed to correct it is not manifest, the Keeper must note the inaccuracy on the entry in question.

(4) Where under subsection (2) the Keeper corrects the record by—

(a) removing the entry from the assignations record, the Keeper must transfer the entry to the archive record and note on the transferred entry—

(i) that the transfer is in consequence of a correction under that subsection, and

(ii) the date and time of the removal, or

(b) removing or replacing data included in the entry or by replacing a copy document, the Keeper must note on the entry—

(i) that it has been corrected, and

(ii) the details of the correction (including, without prejudice to the generality of this paragraph, the date and time of the correction),

and in the case of the replacement of the copy document, must transfer the replaced copy to the archive record and retain it there.

(5) Where under subsection (2) the Keeper effects a correction, the Keeper must notify (in so far as it is reasonable and practicable to do so)—

(a) every person specified for the purposes of this subsection by RoA Rules, and

(b) any other person whom the Keeper considers it appropriate to notify,

that the correction has been effected.

NOTE

Subsections (1) and (2) of this section provide for the Keeper to correct a manifest inaccuracy in the assignations record, where what is needed to correct the inaccuracy is also manifest.

Subsection (3) provides for the Keeper to make a note of the inaccuracy on the entry for the assignation in the assignations record, if what is needed to correct the inaccuracy is not manifest.

Subsections (4) and (5) provide for notification of any correction, and for giving effect to the correction as appropriate in the assignations record or archive record.

See paragraphs 9.10 to 9.22 of the Report.

29 Directions for, or in relation to, correction of the assignations record

(1) Subsection (2) applies where, in any proceedings, a court determines that the assignations record is inaccurate.

(2) The court must direct the Keeper to correct the record.

(3) In connection with any such correction, the court may give the Keeper such further direction (if any) as it considers requisite.

(4) Where by virtue of subsection (2) the Keeper corrects the record by—

(a) removing the entry in question from the assignations record, the Keeper must transfer the entry to the archive record and note on the transferred entry—

(i) that the transfer is in pursuance of the direction of a court under subsection (2), and

(ii) the date and time of the removal, or

(b) removing or replacing data included in the entry or by replacing a copy document, the Keeper must note on the entry—

(i) that it has been corrected, and

(ii) the details of the correction (including, without prejudice to the generality of this paragraph, the date and time of the correction),

and in the case of the replacement of the copy document, must transfer the replaced copy to the archive record and retain it there.

(5) Where by virtue of subsection (2) the Keeper effects a correction, the Keeper must notify (in so far as it is reasonable and practicable to do so)—

(a) every person specified for the purposes of this subsection by RoA Rules, and

(b) any other person whom the Keeper considers it appropriate to notify,

that the correction has been effected.

NOTE

This section provides for a court in appropriate proceedings to be able to direct the Keeper to correct an entry in the RoA, and for the Keeper to comply with such a direction.

Section 118(1) of the Bill sets out that "court" means the Court of Session or the sheriff.

The Bill does not provide for an express right of appeal against, or a review of, a registration decision by the Keeper. An issue relating to the accuracy of the register might be raised in other proceedings, including in a judicial review of such a decision.

Example 1 An assignation document is reduced by the court because it has been forged by one of the purported parties to the document. The court can direct the Keeper to correct the entry in the assignations record.

Example 2 An entry is created in the assignations record for an assignation by P Ltd in favour of Q Ltd. But in the application form for registration of the assignation, Q Ltd erroneously states that Z Ltd is the assignor. Z Ltd could ask the court to correct the entry, although if the inaccuracy is manifest (as is likely) then it might prefer to seek a correction under section 28 of the Bill.

In contrast with section 28 of the Bill, the court does not require to determine whether there is a manifest inaccuracy, or indeed whether what is needed to correct the inaccuracy is manifest. The proper function of the court as provided for by this section is to make a determination, and direct accordingly.

Subsections (4) and (5) provide for notification of any correction, and for giving effect to the correction as appropriate in the assignations record or archive record.

See paragraphs 9.23 to 9.27 of the Report.

30 Proceedings involving the accuracy of the assignations record

The Keeper is entitled to appear and be heard in any civil proceedings, whether before a court or before a tribunal, in which is put in question (either or both)—

(a) the accuracy of the assignations record,

(b) what is needed to correct an inaccuracy in that record.

NOTE

See paragraphs 9.28 to 9.31 of the Report.

31 Correction of assignations record: general

(1) In this Part, any reference to "correction" includes (without prejudice to the generality of that expression and except in so far as the context otherwise requires)—

(a) the removal of data included in an entry,

(b) the removal of an entry from the assignations record and the transfer of that entry to the archive record,

(c) the replacement of data, or of a copy document, included in an entry,

(d) the restoration of data, or of a copy document, to an entry, and

(e) the restoration of an entry (whether or not by removing it from the archive record and transferring it to the assignations record);

and analogous expressions are to be construed accordingly.

(2) A correction is taken to be made on the date and at the time which are entered for it in the register in pursuance of a provision of this Part of this Act.

NOTE

This section deals with some general matters in relation to corrections.

Subsection (1) sets out what is included in a reference to a "correction" in this Part of the Bill.

Subsection (2) sets out that a correction is taken to be made at the date and time for the correction as entered in the RoA. This is particularly important as regards section 26(3) of the Bill, under which an ineffective registration may be made effective by a correction with the result that the claim will transfer. See in that respect paragraphs 9.33 to 9.34 of the Report.

See in general paragraphs 9.8 and 9.9 of the Report.

Searches and extracts

32 Searching the assignations record

(1) Any person may search the assignations record provided that—

(a) the search accords with—

(i) subsection (2), and

(ii) such RoA Rules as are made under section 40(1)(h), and

(b) either—

(i) such fee as is payable for the search is paid, or

(ii) arrangements satisfactory to the Keeper are made for payment of that fee.

(2) The assignations record may be searched only—

(a) by reference to any of the following data in the entries contained in that record—

(i) the names of assignors,

(ii) the names and dates of birth of assignors who are individuals,

(iii) the unique numbers of assignors required by RoA Rules to be identified in the assignations record by such a number,

(b) by reference to registration numbers allocated, under section 23(4)(b), to entries in that record, or

(c) by reference to some other factor, or characteristic, specified for the purposes of this paragraph by RoA Rules.

NOTE

The RoA is a public register (see section 19(1) of the Bill).

Subsection (1) provides for any person to be able to search the assignations record, in accordance with any RoA Rules, and on payment of any fee or the making of arrangements for payment. See paragraphs 10.11 to 10.17 of the Report.

The Bill does not provide expressly for a person to be able to search the archive record. The Scottish Ministers may however make provision to that effect in RoA Rules made under section 40(1)(h) of the Bill. It is also open to any person to obtain from the Keeper an extract of an entry in either the assignations record or archive record under section 35 of the Bill.

Subsection (2) sets out that only such searches in the assignations record as are specified in that subsection, or are specified under RoA Rules, are permitted.

The restriction on searches in the assignations record in this section has two effects.

First, it reduces the risk of identity theft by ensuring that it will not be possible to search against date of birth alone. In addition, the Scottish Ministers will be able to prevent dates of birth from being disclosed by providing in RoA under section 40(1)(i) of the Bill that such dates are not to be available when searching the RoA.

Second, it reduces the risk of unfair commercial practices by not permitting a search against the assignee (typically, a bank or finance company) which might enable a competitor to obtain a list of customers. This is a common feature of personal security regimes based on UCC-9, although the Scottish Ministers will have power to vary that restriction in RoA Rules made under section 40 of the Bill.

See paragraphs 10.2 to 10.10 of the Report.

33 Keeper's duties and powers as regards the provision of facilities for searching the assignations record

(1) The Keeper—

(a) must for the purposes of section 32 provide a search facility the search criteria of which are specified by RoA Rules, and

(b) may provide such other search facilities, with such other search criteria, as the Keeper thinks fit.

(2) In subsection (1), "search criteria" means the criteria in accordance with which what is searched for must match data in an entry in order to retrieve that entry.

NOTE

This section sets out that the Keeper must provide a search facility where the search criteria are as specified in RoA Rules, and may provide for other searches.

See paragraphs 10.22 to 10.29 of the Report.

34 Assignations record: printed search results and their evidential status

A printed search result which relates to a search carried out by means of a search facility provided by the Keeper and which purports to show an entry in the assignations record is admissible in evidence and, in the absence of evidence to the contrary, is sufficient proof of—

(a) the registration of the assignation document to which the result relates,

(b) a correction of the entry in the assignations record to which the result relates, and

(c) the date and time of such registration or correction.

NOTE

This section provides for printed search results obtained from the Keeper to be used as evidence of certain matters and, moreover, to prove certain matters unless there is evidence to the contrary.

This section should be read with section 35, which provides for an extract from the RoA, which will provide sufficient evidence of the contents of the relevant entry at the date the extract is issued. It cannot be rebutted by other evidence: but see the liability of the Keeper for errors in extracts under section 37(1)(d) of the Bill.

See paragraphs 10.30 and 10.31 of the Report.

35 Register of Assignations: extracts and their evidential status

(1) Any person may apply to the Keeper for an extract of an entry in the register.

(2) The Keeper must issue the extract if either—

(a) such fee as is payable for issuing it is paid, or

(b) arrangements satisfactory to the Keeper are made for payment of that fee.

(3) The Keeper may validate the extract as the Keeper considers appropriate.

(4) The Keeper may issue the extract as an electronic document if the applicant does not request that it be issued as a traditional document.

(5) The extract is to be accepted for all purposes as sufficient evidence of the contents of the entry as at the date on which and the time at which the extract is issued (being a date and time specified in the extract).

NOTE

This section enables any person to obtain from the Keeper an extract of any entry or part of an entry in the RoA, on payment of any fee (or making an arrangement to pay). An extract is sufficient evidence of the contents of an entry at the time the extract is issued, and can be used for the purpose of proving a fact in any court or tribunal proceedings.

See paragraphs 10.32 to 10.34 of the Report.

Request for information

36 Assignee's duty to respond to request for information

(1) An entitled person may request the person identified in an entry in the assignations record as the assignee (the person so identified being in this section referred to as "IA") to provide the entitled person with a written statement as to whether—

(a) a claim specified by the entitled person is assigned by the assignation document, or

(b) a condition—

(i) so specified, and

(ii) to which the assignation is, under section 2(1), made subject,

has been satisfied.

(2) The following are entitled persons for the purposes of this section—

(a) in relation to a request under subsection (1), a person who (depending on who holds the claim) may have a right to execute diligence against the claim, or

(b) a person not mentioned in paragraph (a) but who—

(i) is prescribed under this paragraph, or

(ii) has the consent of the person identified in the entry as the assignor to make a request under paragraph (a) or (b) of subsection (1).

(3) The reference in subsection (2)(a) to "a person who (depending on who holds the claim) may have a right to execute diligence against the claim" includes a reference to a person authorised to execute a charge for payment who (depending on who holds the claim) may have a right to execute diligence against the claim if and when the days of charge expire without payment.

(4) Subject to subsection (6), IA must, within 21 days after receiving a request by virtue of subsection (1), comply with that request unless subsection (8) applies.

(5) IA may recover from the entitled person any costs reasonably incurred in complying with the request.

(6) The court, if satisfied that in all the circumstances it would be unreasonable to require IA—

(a) to comply with the request (whether in whole or in part), may by order, on the application of IA, exempt IA from complying with—

(i) the request, or

(ii) such part of the request as it may specify in the order, or

(b) to comply with the request within the 21 days mentioned in subsection (4), may by order, on such application, extend by such number of days as it may specify in the order the period within which IA must comply with the request.

(7) If the court is satisfied, on the application of the entitled person, that IA has, without reasonable excuse, failed to comply with subsection (4), it may by order require IA to comply with the request within 14 days.

(8) This subsection applies—

(a) where it is manifest that the registration is ineffective as regards the assignation of the claim to which the request relates,

(b) in the case of a claim specified under subsection (1)(a) (and without prejudice to the generality of paragraph (a)), where it is manifest from the entry for the assignation that the claim is not assigned by the assignation document, or

(c) where—

(i) IA has, within the 3 months immediately preceding IA's receipt of the request, complied with a request under the same paragraph of subsection (1), by the same person and in relation to the same claim, and

(ii) the information contained in the statement issued in relation to the earlier request is still correct.

NOTE

This section provides for an entitled person, as specified in subsections (2) and (3), to be able to request information about a claim from the person identified as the assignee in the assignations record. The request does not require to be in writing, but the response does.

Subsection (1) sets out that the information that may be requested is, first, whether a particular claim is assigned by the assignation and, second, whether a condition to which the assignation is subject has been satisfied. The right to request these types of information is of particular importance where a claim is assigned before it is held by the assignor (a "future" claim). See paragraphs 11.2 to 11.10 of the Report.

Subsections (2) and (3) have the effect that an entitled person is:

(a) a person who has (or may have) a right to execute diligence against the claim,

(b) a person who has the consent of the assignor to make the request, and

(c) any other person prescribed by the Scottish Ministers (see section 118(1) of the Bill for the definition of "prescribed").

Subsection (4) gives the person named as assignee in the assignations record 21 days to respond, except where subsection (8) applies. See paragraphs 11.11 to 11.17 of the Report.

Subsection (5) allows the reasonable costs of responding to the request to be charged to the person making the request. See paragraph 11.16 of the Report.

Subsection (6) gives the court power either to exempt the person named as assignee from complying with the request, or to grant further time. For example, and depending on the circumstances, 21 days may be too short a period to assemble the necessary information.

Subsection (7) enables the court to order the person named as assignee to comply with the request for information without delay.

Subsection (8) excuses the person named as assignee from providing information in certain circumstances, namely:

(a) where the position as to whether the claim has been assigned is clear from the register, or

(b) where the information has been given within the last three months, and it has not changed.

The effect of this section is that persons with a legitimate interest in a claim that may be the subject of an assignation will be able to obtain information that might not otherwise be available by searching the RoA. Information provisions of this type are a common feature of UCC-9 and the PPSA regimes.

Example — D Ltd is a plumbing business. It assigns its "future" customer invoices to B Ltd to be identified on schedules to be sent to B Ltd. D Ltd becomes insolvent. Its liquidator requires to see whether certain invoices have been assigned, and makes an information request under this section.

Entitlement to compensation

37 Register of Assignations: liability of Keeper

(1) A person is entitled to be compensated by the Keeper for loss suffered in consequence of—

(a) an inaccuracy attributable to the Keeper—

(i) in the making up, maintenance or operation of the register, or

(ii) in an attempted correction of the register,

(b) the issue, under section 24(1), of a written statement which is incorrect,

(c) the service, under section 28(5) or 29(5), of a notification which is incorrect, or

(d) the issue, under section 35, of an extract which is not a true extract.

(2) But the Keeper has no liability under subsection (1)—

(a) in so far as the person's loss could have been avoided had the person taken measures which it would have been reasonable for the person to take,

(b) in so far as the person's loss is not reasonably foreseeable, or

(c) for non-patrimonial loss.

NOTE

This section provides for the Keeper to compensate any person who has suffered a loss in consequence of a matter specified in subsection (1).

Liability under subsection (1) is strict, in that the person does not have to show that the Keeper is at fault. However, subsection (2) limits the losses that can be recovered by excluding certain types of claim. The limitation is similar to that in section 106 of the Land Registration etc. (Scotland) Act 2012.

See paragraphs 11.22 to 11.34 of the Report.

38 Register of Assignations: liability of certain other persons

(1) Where a person (in this section referred to as "P") suffers loss in consequence of—

(a) an inaccuracy in an entry in the register (not being an inaccuracy attributable to the Keeper), P is entitled to be compensated for that loss by the person who made the application which gave rise to the entry if, in making it, that person failed to take reasonable care,

(b) an inaccuracy in information supplied in response to a request under section 36(1), P is entitled to be compensated for that loss by the person who supplied the information if, in supplying it, that person failed to take reasonable care, or

(c) a failure, without reasonable cause, to comply with a request under section 36(4), P is entitled to be compensated for that loss by the person whose failure it was.

(2) But a person has no liability under subsection (1)—

(a) in so far as P's loss could have been avoided had P taken measures which it would have been reasonable for P to take,

(b) in so far as P's loss is not reasonably foreseeable, or

(c) for non-patrimonial loss.

NOTE

This section provides for certain persons to be liable, on fault shown, for losses suffered by another person in consequence of a matter specified in subsection (1).

Subsection (1)(a) applies where a person suffers loss as a result of an inaccuracy in an entry, where the person who made the application which led to the entry did not exercise reasonable care.

Example — Bruce maliciously registers a forged assignation bearing to be granted by Claire in an effort to affect her credit rating. Claire has a claim against Bruce if she suffers loss.

Subsection (1)(b) applies where, as a result of a failure to take reasonable care, there is an inaccuracy in responding to an information request under section 36 of the Bill.

Example — Information is supplied by Brian that a certain claim is not carried by an assignation from Andrew to Brian. But Brian does not take reasonable care, and the information is wrong. The person who receives the information then takes what will be an invalid assignation of the claim from Andrew, because it has already been transferred to Brian. That person will have a claim against Brian.

Subsection (1)(c) applies where a person has failed, without reasonable cause, to provide information under section 36 of the Bill.

Example — Alan has granted an assignation of certain claims to Bob. The Selkirk Bank is considering whether or not to lend money to Alan, and seeks information from Bob with the consent of Alan about which claims are assigned. Bob does not comply, and the Bank obtains a court order. Bob still does not comply, and the Bank decides not to make the loan. Alan has a claim against Bob for loss suffered due to being unable to obtain a loan from the Bank.

Subsection (2) imposes the same restrictions on liability as those set out in section 37(2) of the Bill.

See paragraphs 11.35 to 11.42 of the Report.

Service of documents for purposes of certain sections of this Chapter of Part 1

39 Service of documents for purposes of certain sections of this Chapter of Part 1

In the application of section 26 of the Interpretation and Legislative Reform (Scotland) Act 2010 (service of documents) for the purposes of section 28(5), 29(5) or 36(1)—

(a) subsection (4) of that section of that Act is to be construed as if, for paragraphs (a) to (c) of the subsection, there were substituted the words "the address given for the person in the entry in question", and

(b) where an e-mail address for the person identified as the assignee is contained in the entry in question, the demand, request or notice is to be taken to be served as mentioned in subsection (2)(c) of that section of that Act on being transmitted to the e-mail address.

NOTE

Section 26 of the Interpretation and Legislative Reform (Scotland) Act 2010 makes provision in relation to the service (including sending) of documents for the purpose of measures in an Act of the Scottish Parliament.

This section modifies those provisions for the purposes of certain provisions in Chapter 1 of Part 1 of the Bill.

Paragraph (a) refers to subsection (4) of section 26, which deals with the sending of notices. The effect of paragraph (a) is that a notice should be sent to the address for the person that is given in the entry in the assignations record.

Paragraph (b) refers to subsection (2)(c) of section 26, which deals with electronic communication of notices. The effect of paragraph (b) is that where an e-mail address is given for a person in the entry in the assignations record, the communication should be to that address.

RoA Rules

40 RoA Rules

(1) The Scottish Ministers may by regulations make rules (in this Act referred to as "RoA Rules")—

(a) as to the making up and keeping of the register,

(b) as to procedure in relation to applications—

(i) for registration, or

(ii) for corrections,

(c) as to the identification, in any such application and in the register, of any person or claim, including—

(i) how the proper form of a person's name is to be determined, and

(ii) where the person bears a number (whether of numerals or of letters and numerals) unique to the person, whether that number must (or may) be used in identifying the person,

(d) as to the degree of precision with which time is to be recorded in the register,

(e) as to the manner in which an inaccuracy in the assignations record may be brought to the attention of the Keeper,

(f) as to information which, though contained in an assignation document, need not be included in a copy of that document submitted with an application under section 23,

(g) as to whether a signature contained in an assignation document need be included in a copy of that document so submitted,

(h) as to searches in the register,

(i) as to data which, though contained in the register, is not to be—

(i) available to persons searching it, or

(ii) included in any extract issued under section 35,

(j) prescribing the configuration, formatting and content of—

(i) applications,

(ii) notices,

(iii) documents,

(iv) data,

(v) statements, and

(vi) requests,

to be used in relation to the register,

(k) as to when the register is open for—

(i) registration, and

(ii) searches,

(l) requiring there to be entered in the assignations record or the archive record such data as may be specified in the rules, or

(m) regarding other matters in relation to registration under this Part, being matters for which the Scottish Ministers consider it necessary or expedient to provide in order to give full effect to the purposes of this Part.

(2) Before making RoA Rules the Scottish Ministers must consult the Keeper.

NOTE

This section sets out that the Scottish Ministers may, by regulations, make rules (RoA Rules) providing for the operation of the Register of Assignations. They must consult the Keeper before doing so.

The power to make RoA Rules includes the powers in paragraphs (f) and (g) of subsection (1) to authorise the redaction of information or signatures from an entry in the RoA, and the power in paragraph (i) to make certain information unavailable to searchers (which might include an individual's date of birth).

See paragraphs 11.43 to 11.49 of the Report.

CHAPTER 3

MISCELLANEOUS AND INTERPRETATION OF PART 1

Miscellaneous

41 Repeal of Transmission of Moveable Property (Scotland) Act 1862

The Transmission of Moveable Property (Scotland) Act 1862 is repealed.

NOTE

The Transmission of Moveable Property (Scotland) Act 1862 makes provision for intimation of claims, is superseded by the Bill, and is therefore repealed by this section.

Interpretation of Part 1

42 Interpretation of Part 1

(1) In this Part (except where the context otherwise requires)—

"the archive record" is to be construed in accordance with section 22,

"assignation" means an assignation under section 1(1),

"assignation document" has the meaning given to that expression by section 1(1),

"the assignations record" is to be construed in accordance with section 21(2),

"assignee"—

(a) is to be construed in accordance with section 1(2)(b), and

(b) without prejudice to the generality of the expression, may consist of two or more co-assignees,

"assignor"—

(a) is to be construed in accordance with section 1(2)(a), and

(b) without prejudice to the generality of the expression, may consist of two or more co-assignors,

"the register" is to be construed in accordance with section 19(2), and

"RoA Rules" has the meaning given to that expression by section 40(1).

(2) In this Part, a reference to a "claim"—

(a) is to a right to the performance of an obligation, but

(b) does not include a reference to—

(i) a non-monetary right relating to land, or

(ii) a negotiable instrument.

(3) In this Part, "right in security"(except where the context otherwise requires)—

(a) means a right in security over property and includes a floating charge, but

(b) does not include a right to execute diligence.

(4) Without prejudice to the generality of paragraph (a) of subsection (2), in that paragraph "performance" includes the fulfilment of an obligation not to do something.

(5) Any reference, however expressed, in this Part to registering an assignation document, is to be construed as a reference to the Keeper's carrying out the duties imposed on the Keeper by section 23(4).

(6) Any reference in this Part to the "proper name" of a person is to that person's name in the form determined in accordance with rules under section 40(1)(c)(i).

(7) There is an "inaccuracy" in the assignations record where—

(a) data included, by virtue of section 21(1), in an entry in the record is inaccurate,

(b) an entry in the record—

(i) does not include a copy of the assignation document as required by paragraph (h) of that section, or

(ii) includes such a copy but the document copied is invalid, or

(c) an entry has incorrectly been removed from that record.

NOTE

This section defines key terms used in this Part of the Bill.

Subsection (2) defines "claim" as the right to the performance of an obligation, but excluding for that purpose both non-monetary rights relating to land and negotiable instruments. See paragraph 4.16 of the Report.

Subsection (3) makes it clear that the references in the Bill to "right in security" mean a right in security over property. The meaning of the expression is therefore limited to "true" securities where the secured creditor has a subordinate real right in the asset.

A right in security includes a floating charge, but does not include a right to execute diligence in satisfaction of sums due under a court order (or equivalent).

Subsection (4) confirms that "performance" includes the fulfilment of negative obligations.

PART 2

SECURITY OVER MOVEABLE PROPERTY

CHAPTER 1

PLEDGE

Pledge, secured obligation and encumbered property

43 Pledge

(1) A pledge is a right in security over moveable property.

(2) A pledge is created over—

(a) corporeal property—

(i) by delivery of the property to the person in whose favour the pledge is granted provided that the property is the provider's at the time of delivery, or

(ii) in a case where the property is not the provider's at the time of such delivery, on the property becoming the provider's subsequent to such delivery,

(b) corporeal or incorporeal property (or property which is both corporeal and incorporeal), by registration in accordance with section 48 or 49.

(3) Without prejudice to the application of subsection (2) as respects the creation of a pledge over a financial instrument, a pledge may be created over a financial instrument in a way mentioned in section 50(2)(a).

(4) A pledge created by registration in accordance with section 48 or 49 or in a way mentioned in section 50(2)(a) is to be known as a "statutory pledge".

(5) In this Part—

(a) the person in whose favour the pledge is granted is referred to as the "secured creditor", and

(b) the person who grants the pledge is referred to as the "provider".

(6) Nothing in subsection (2)(a) affects any rule of law in relation to a pledge over a negotiable instrument.

NOTE

Subsection (1) confirms that a pledge is a type of right in security over moveable property.

Subsection (2) sets out the main methods by which a pledge is created over corporeal and incorporeal moveable property respectively. See paragraphs 21.1 to 21.3 of the Report.

Corporeal moveable property is property that has physical form, other than land or buildings (which are known as heritable property). It includes whisky, paintings, furniture, and motor vehicles.

Incorporeal moveable property is property that does not have physical form, such as intellectual property or financial instruments.

The Bill defines corporeal moveable property, but only to confirm that it does not include money for the purposes of the Bill (see section 116(1) which defines "money" by reference to section 175 of the Bankruptcy and Diligence etc. (Scotland) Act 2007, with the effect that it means cash and banking instruments (such as cheques and postal orders)).

A pledge over corporeal moveable property, sometimes known as a possessory pledge, is with one exception created by delivery of the property to the secured creditor (for which see section 45 of the Bill).

The exception is that where the property is not the provider's when delivered then the pledge is created when the property becomes the provider's.

A pledge over corporeal moveable property can, and a pledge over incorporeal moveable property must (with one exception), be created by registration in the new Register of Statutory Pledges.

Subsection (3) sets out that the exception is for a pledge that evidences a financial collateral arrangement in respect of a financial instrument, for which see section 50 of the Bill.

Section 117 of the Bill has the effect that a reference to registering (however expressed) is a reference to registration of a pledge by the Keeper in the Register of Statutory Pledges under sections 91 and 92 of the Bill.

Subsection (6) sets out that nothing in subsection (2)(a) (creation of a possessory pledge) affects any rule of law in relation to a pledge over a negotiable instrument such as a bill of exchange or cheque.

See also paragraphs 19.8, 19.13 to 19.15, 19.31 to 19.35, and 22.59 to 22.60 of the Report.

44 Secured obligation and encumbered property

(1) The obligation secured by a pledge is referred to in this Part as the "secured obligation".

(2) The secured obligation—

(a) may be any obligation owed, or which will or may become owed,

(b) need not be an obligation owed—

(i) by the provider, or

(ii) to the secured creditor, and

(c) includes ancillary obligations owed (as for example to pay interest, damages and the reasonable expense of extra-judicial recovery of interest or damages).

(3) The property over which a subsisting pledge has been created (and in respect of which that pledge subsists)—

(a) is referred to in this Part as the "encumbered property", and

(b) except in so far as the provider and the secured creditor agree otherwise, includes the natural fruits, but not the incorporeal fruits, of the property.

(4) And that property must, at the time the pledge is created, be transferable (whether or not its transferability is restricted in some way).

(5) Subsection (3)(b) is without prejudice to sections 75 and 76.

NOTE

Subsection (1) sets out that the obligation secured by a pledge is referred to in the Bill as a "secured obligation".

Subsection (2) makes provision for the secured obligation. See paragraphs 19.16 to 19.26 of the Report.

Subsection (2)(a) provides that a pledge can cover both present and future obligations, as is the case for example with a standard security over land or buildings (see section 9(8)(c) of the Conveyancing and Feudal Reform (Scotland) Act 1970 in respect of obligations that can be secured on such heritable property). The effect is that it is competent to grant a pledge securing all sums due and to become due to the creditor.

Subsection (2)(b) provides, first, that a pledge can secure third party debt.

Example George has an overdraft with the Iron Bank, and the Bank is willing to accept a pledge as security for the debt. But George does not have moveable property of any value, so his friend Holly agrees to pledge her car. Holly is thus a third party providing security for the loan by the Bank to George.

Subsection (2)(b) provides, second, that the secured obligation may be owed to a party other than the secured creditor. This would be the case where, for example, the secured creditor is a security trustee.

Subsection (2)(c) is influenced by the DCFR IX.–2:401(1), and provides that ancillary obligations are secured by a pledge. The typical ancillary obligation is interest on a debt, but the pledge will cover other obligations such as any obligation to pay the creditor damages for a loss they have suffered (important where non-monetary obligations are secured). A pledge might also secure costs arising from the extra-judicial recovery of interest or damages, such as interest due for the late payment of debts for the purposes of Directive 2000/35/EC on combating late payment in commercial transactions (OJ L 200, 8.8.2000, p 35).

Subsection (3)(b) gives statutory effect to a general rule of law. Unless agreed otherwise, the secured creditor is entitled to the natural fruits of the encumbered property (such as the young of animals), but not entitled to the civil fruits (such as dividends on shares, or rent payments). See paragraphs 19.65 to 19.71 of the Report.

Subsection (4) provides that the encumbered property must be transferable. This reflects general security law, as a security over a non-transferable right has no practical value (as the property could not be sold to satisfy the secured obligation). Sometimes - notably in the case of certain intellectual property licences - the property is transferable subject to restrictions, and it will be possible to take security over such property. See paragraphs 19.62 and 19.63 of the Report.

Subsection (5) provides that the default rule set out in subsection (3)(b) is without prejudice to the secured creditor's right to enforce the security by leasing or licensing the property, and applying the rents or royalty payments to the debt.

Possessory pledge

45 Delivery

(1) For the purposes of section 43(2)(a), delivery must be effected—

(a) by—

(i) physically handing over, or

(ii) giving control of,

the property to the secured creditor or to a person authorised to accept delivery on behalf of the secured creditor,

(b) by giving control of the premises in which the property is located to the secured creditor or to a person so authorised,

(c) by instructing an independent third party who has direct possession or custody of the property to hold the property on behalf of the secured creditor or of a person so authorised, or

(d) by delivering a bill of lading representing the property to the secured creditor or to a person so authorised (and where that bill is to the order of a particular person, by procuring the endorsement of the bill in favour of the secured creditor).

(2) Property already in the direct possession or custody—

(a) of the secured creditor, or

(b) of a person authorised to hold the property on behalf of the secured creditor,

when agreement on the creation of the pledge is reached between the provider and the secured creditor, is deemed to have been delivered in accordance with section 43(2)(a).

(3) This section is without prejudice to section 2 of the Factors Act 1889.

NOTE

This section reforms and codifies the law on delivery of property to a secured creditor for the purpose of creating a possessory pledge.

Subsection (1) sets out four options for effecting delivery, at which time the pledge will be created. It makes clear, contrary to the decision in *Hamilton v Western Bank* (1856) 19 D 152, that delivery for the purpose of creating a pledge of corporeal moveable property is not restricted to physical delivery.

Subsection (1)(a) provides for physical delivery, either to the secured creditor or to their representative.

Example Peter might decide to offer a watch as security for a loan from Renata, and will create the pledge by handing her the watch for that purpose.

Subsection (1)(b) provides for delivery by means of giving control of the premises in which the encumbered property is kept.

Example Sean might decide to offer his yacht as security for a loan from Teddy, and will create the pledge by giving Teddy the only key to the boathouse in which it is stored.

Subsection (1)(c) provides for constructive delivery by means of an instruction to a third party holder of the property.

Example Ulrike has stored whisky in a warehouse owned by Val. She decides to offer the whisky as security for a loan by Zebedee. Delivery is effected, and the pledge created, if Ulrike instructs Val to hold the whisky on behalf of Zebedee.

Subsection (1)(d) provides for symbolic delivery by means of delivery of a bill of lading for the property, such as cargo aboard a ship as represented by the bill of lading. A bill is a document of title, and will where necessary require to be endorsed in favour of the secured creditor.

Subsection (2) provides that delivery is not required if the property is already in the direct possession or custody of the prospective secured creditor.

Example Joan has borrowed Karen's bicycle. Karen agrees that the bicycle can be pledged as regards a debt owed by her to Joan. The pledge is created when the agreement is made.

Subsection (3) confirms that section 2 of the Factors Act 1889 (which allows mercantile agents to pledge goods by means of handing over documents of title) continues to apply. A mercantile agent, as defined in section 1 of that Act, is an agent having in the customary course of business authority to sell goods, to consign goods for the purpose of sale, to buy goods, or to raise money on the security of goods.

See paragraphs 25.2 to 25.10 of the Report.

Statutory pledge

46 Constitutive document

(1) A statutory pledge requires a constitutive document.

(2) The constitutive document must—

(a) be executed or authenticated by the provider,

(b) identify the property which is to be the encumbered property, and

(c) identify the secured obligation.

(3) For the purposes of subsection (2)(b), the property identified may either be property of, or property to be acquired by, the provider.

(4) Without prejudice to section 52(2), if the encumbered property is to consist of more than one item the constitutive document need not identify each item separately provided that the document identifies the items in terms of their constituting an identifiable class.

NOTE

This section is the first of 18 sections (sections 46 to 63) that make provision for a statutory pledge. This type of pledge does not require delivery of the encumbered property, and is therefore a non-possessory pledge.

Subsection (1) provides that a statutory pledge must have a constitutive document, so that it is not competent to grant an oral non-possessory pledge. There is no equivalent rule for a possessory pledge as a security of that type is created by delivery of the encumbered property.

Subsection (2) requires that the constitutive document is subscribed by the provider using a physical signature ("executed") or signed electronically ("authenticated"). Section 118(1) of the Bill defines "executed" and "authenticated" for that purpose. There is however an exception to that general rule for documents that evidence a security financial collateral arrangement in respect of a financial instrument, for which see section 50(5) of the Bill.

Subsections (2) and (4) also set out that the document must identify the encumbered property, including by reference to an identifiable class of property (for example, "my computers"), or by reference to a description in another document. This is however subject to section 53(2) of the Bill which has the effect that an individual must generally identify each asset to be subject to the pledge. See in general paragraphs 23.4 to 23.10 of the Report.

An entitled person, as defined in section 110(2) of the Bill, is able to obtain from the secured creditor further information in respect of the encumbered property by making a request to that effect under that section.

Subsection (3) makes it clear that a statutory pledge may be granted over property not owned by the provider at the time the property is identified in the document. This subsection should be read with section 48 of the Bill which has the effect that the pledge is not created until (and if) the property is the provider's property.

47 Competence of creating statutory pledge over certain kinds of property

(1) It is not competent to create a statutory pledge over corporeal property if that property is—

(a) an aircraft in respect of which it is competent to register a mortgage in the Register of Aircraft Mortgages kept by the Civil Aviation Authority,

(b) an aircraft object (as defined in regulation 5 of the International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015 (S.I. 2015/912)), or

(c) a ship (or a share in a ship) in respect of which it is competent to register a mortgage in the register of British ships maintained for the United Kingdom under section 8 of the Merchant Shipping Act 1995.

(2) It is not competent to create a statutory pledge over incorporeal property unless that property is—

(a) intellectual property,

(b) an application for, or licence over, intellectual property,

(c) a financial instrument, or

(d) of such other kind as may be prescribed.

NOTE

This provision sets out the types of moveable property in respect of which it is not competent to grant a statutory pledge.

Subsection (1) has the effect that a statutory pledge is not competent in respect of property that is subject to the alternative security regimes specified in that subsection:

(a) For aircraft and for certain ships (and shares in ships) it is possible to create an aircraft or ship mortgage (see paragraphs 21.7 to 21.12 of the Report), and

(b) For aircraft objects it is possible to create an international interest under the Cape Town Convention as implemented - following ratification by the United Kingdom on 27 July 2015 - by the International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015 (S.I. 2015/912) (and see paragraphs 21.16 to 21.20 of the Report).

The Cape Town Convention is an international treaty intended to standardise security transactions involving certain types of moveable property, and it creates in particular international standards for security interests, and various legal remedies for default in financing agreements (including repossession).

Subsection (2) limits the scope of a statutory pledge over incorporeal moveable property to the types of property listed in paragraphs (a) to (c) of that subsection. See paragraphs 22.25 to 23.34, and paragraph 22.62, of the Report.

Subsection (2) has the effect of excluding all other types of incorporeal moveable property from the scope of the pledge, unless the property is of a type prescribed by regulations by the Scottish Ministers (see sections 116(1) and 118(1) of the Bill for the definitions of "financial instrument" and "prescribed" respectively).

48 Creation of statutory pledge by registration: general

(1) A statutory pledge is created over property on the requirements mentioned in subsection (2) all being met.

(2) Those requirements are that—

(a) the property is the provider's,

(b) the statutory pledge is registered, and

(c) the property is identifiable as property to which the constitutive document relates.

(3) Subsection (1) is without prejudice to sections 46(2) and 49(1).

(4) This section is subject to sections 50(2)(a), 51 and 95.

NOTE

Subsection (1) has the principal effect that a statutory pledge is created by registration of the constitutive document in the Register of Statutory Pledges (see section 117 of the Bill for the meaning of references to "registering" or similar expressions).

In addition, as set out in subsection (2), the property must be the provider's property, and it must be identifiable as property subject to the pledge. The pledge is only created when each of the requirements in that subsection is met, regardless of which occurs first. See paragraphs 23.19 and 23.21 to 23.27 of the Report.

It follows for example that a pledge is not created at the time of registration if the property is not the provider's at that time.

Example — Adam grants a pledge in June to the Haddington Bank over motor vehicles he has recently acquired, to be listed in a schedule to be given to the Bank. The Bank registers the pledge in the RSP in July. Adam sends the schedule to the Bank in August. The statutory pledge is created in August when all three conditions in subsection (2) are met.

Subsections (3) and (4) qualify the effect of this section in four respects:

(a) Subsection (1) is without prejudice to section 49(1) of the Bill, with the effect of clarifying that property can be added to the pledge by means of an amendment document.

(b) The section is subject to section 50(2)(a) of the Bill, with the effect that a statutory pledge over a financial instrument can be created coming into the possession of, or under the control of, a collateral-taker.

(c) The section is subject to section 51 of the Bill, with the effect that a pledge over property yet to be acquired may be ineffective if the property is acquired after the provider becomes insolvent.

(d) The section is subject to section 95 of the Bill, with the effect that registration is ineffective if the entry in the statutory pledges record kept under section 89 of the Bill does not include a copy of the constitutive document or has a seriously misleading inaccuracy.

49 Creation of statutory pledge over added property

(1) Subsection (2) applies where a statutory pledge is amended so as to add property to the encumbered property.

(2) The statutory pledge is created over the added property on the requirements mentioned in subsection (3) all being met.

(3) Those requirements are that—

(a) the added property is the provider's,

(b) the amendment is registered, and

(c) the added property is identifiable as property to which the amendment document relates.

(4) This section is subject to sections 50(2)(a), 51 and 96.

(5) Subsection (2) is without prejudice to section 60(1).

NOTE

This section provides for the creation of the security over property added to a statutory pledge.

Subsection (3) has the same effect for property added to a pledge by an amendment document as section 48(2) has for property identified in the constitutive document.

Subsection (4) sets out that this section is subject to sections 50(2)(a) and 51 of the Bill (dealing with financial instruments and insolvency respectively), and to section 96 of the Bill which sets out that registration is ineffective if the entry in the statutory pledges record does not include a copy of the amendment document or has an inaccuracy which is seriously misleading.

See paragraphs 23.21 to 23.27, and 23.33 to 23.40, of the Report.

50 Creation of statutory pledge over financial instrument

(1) Subsection (2) applies if a constitutive document, or an amendment document, evidences a security financial collateral arrangement in respect of a financial instrument.

(2) A statutory pledge is created over the financial instrument either—

(a) on the requirements mentioned in subsection (3) all being met, or

(b) as mentioned in, as the case may be, section 48 or 49.

(3) Those requirements are that—

(a) the instrument is the property of the provider,

(b) the instrument is in the possession, or under the control, of the collateral-taker or of a person authorised to act on the collateral-taker's behalf, and

(c) the instrument is identifiable as an instrument to which the constitutive document, or amendment document, relates.

(4) If a statutory pledge is created by virtue of subsection (2)(a), the requirements of section 46(2), or as the case may be of section 60(1), as to execution or authentication do not apply.

(5) Without prejudice to the generality of subsection (1), for the purposes of that subsection a constitutive document, or an amendment document, may be evidenced—

(a) in writing transcribed by electronic or other means in a durable medium, or

(b) in sounds recorded in such a medium.

(6) This section is to be construed as one with regulation 3 of the Financial Collateral Arrangements (No. 2) Regulations 2003 (S.I. 2003/3226).

NOTE

This section provides for statutory pledges over financial instruments in respect of a security financial collateral arrangement ("SFCA") for the purposes of the Financial Collateral Arrangements (No. 2) Regulations 2003 (S.I. 2003/3226). The 2003 Regulations implement Directive 2002/47/EC on financial collateral arrangements (OJ L 168. 6.6.2002, p 43). See section 116(1) of the Bill for the definition of "financial instrument".

The parties to a SFCA must both be non-natural persons, with the effect that this section will not apply to a pledge by an individual provider.

Subsections (2) and (3) have the effect that a statutory pledge in respect of a SFCA can be created by registration, as for any other statutory pledge, or by the encumbered property (the collateral) coming into the possession or under the control of the secured creditor.

Subsection (4) removes the need for a constitutive or amendment document for the purposes of a SFCA to be executed or authenticated, in order to comply with the 2003 Regulations.

Subsection (5) extends the methods by which a constitutive or amendment document for the purposes of a SFCA may be evidenced, also in order to comply with the 2003 Regulations.

See paragraphs 22.25 to 22.34, and 37.3 to 37.5, of the Report.

51 Creation of statutory pledge: insolvency

(1) Subsection (2) applies where, after a statutory pledge is granted, the provider becomes insolvent.

(2) The statutory pledge is not created over any property which, though identified by the constitutive document (or by an amendment document) as property to be encumbered, is not acquired by the provider before the provider becomes insolvent.

(3) For the purposes of subsection (2)—

(a) a provider who is an individual, or the estate of which may be sequestrated by virtue of section 6 of the Bankruptcy (Scotland) Act 2016, becomes insolvent when—

(i) the provider's estate is sequestrated,

(ii) the provider grants a trust deed for creditors or makes a composition or arrangement with creditors,

(iii) a voluntary arrangement proposed by the provider is approved, or

(iv) the provider's application for a debt payment programme is approved under section 2 of the Debt Arrangement and Attachment (Scotland) Act 2002, and

(b) a provider other than is mentioned in paragraph (a) becomes insolvent when—

(i) a decision approving a voluntary arrangement entered into by the provider has effect under section 4A of the Insolvency Act 1986,

(ii) the provider is wound up under Part 4 or 5 of that Act of 1986 or under section 367 of the Financial Services and Markets Act 2000,

(iii) an administrative receiver, as defined in section 251 of that Act of 1986, is appointed over all or part (being a part to which the constitutive document or any amendment document relates) of the property of the provider, or

(iv) the assignor enters administration ("enters administration" being construed in accordance with paragraph 1(2) of schedule B1 of that Act of 1986).

(4) The Scottish Ministers may by regulations amend—

(a) any sub-paragraph of subsection (3)(a) or (b) (including any sub-paragraph added to that subsection by virtue of paragraph (b)), or

(b) subsection (3)(a) or (b) by adding sub-paragraphs which specify further circumstances in which a person becomes insolvent.

NOTE

Sections 46(3) and 60(3) of the Bill set out that the property to be encumbered as described in the constitutive document of a statutory pledge, or an amendment document in respect of the pledge, may be property to be acquired by the provider of the pledge.

This section provides for the effect of the intervening insolvency of the provider by setting out that a statutory pledge will not be created over property acquired at a time when the provider is insolvent, as specified in this section.

The effect is that the property in question is treated as an asset of the provider for the purposes of the insolvency. It may for example be sold or realised for the benefit of the creditors as a whole.

Subsection (4) confers a power on the Scottish Ministers to amend subsection (3) by regulations. That power could for example be used to add a further type of insolvency to the list in subsection (3), such as an equivalent foreign insolvency.

See paragraphs 23.28 to 23.32 of the Report.

52 Providers who are individuals

(1) Subsections (2) to (4) apply where the provider of a statutory pledge is an individual.

(2) The encumbered property must consist only of assets separately identified in the constitutive document (or in any amendment document) and either—

(a) be the provider's property as at the time the document in question is granted, or

(b) be acquired by the provider after that time if—

(i) the acquisition is financed by credit, and

(ii) an obligation to repay that credit is the secured obligation.

(3) A corporeal asset so identified must, immediately before the document in question is granted, have a monetary value exceeding—

(a) £1,000, or

(b) such other amount as may be prescribed for the purposes of this subsection.

(4) Except that, where the provider is a sole trader, subsections (2) and (3) are to be disregarded as respects any assets used, or to be used, wholly or mainly for the purposes of the provider's business.

NOTE

This section provides debtor protections for individuals granting a statutory pledge over their personal property.

This section sets out that the protections do not apply where the individual is a sole trader, and the pledge is over assets used wholly or mainly for the purposes of the trader's business.

The protections in this section complement the provisions of the Consumer Credit Act 1974, which apply to the grant of any security right by an individual (as defined for the purpose of that Act in section 189(1) of the Act).

Subsection (2) sets out that the assets must be separately identified in the constitutive document and any amendment document. It would not therefore be competent for an individual to grant a statutory pledge by reference to a class of property such as "my books" or "the contents of my garage".

In addition, subsection (2) has the effect that an individual may not normally grant a statutory pledge over an asset he or she has yet to acquire. An exception to this general rule applies where the individual is supplied with credit for the purchase, and the secured obligation is the obligation to repay that credit. Thus where a motor vehicle is to be acquired, a statutory pledge can be granted over that vehicle, to secure funding for the purchase.

Subsection (3) provides that the property to be pledged must have a monetary value exceeding £1,000 (or such other sum as may be prescribed by regulations made by the Scottish Ministers). The effect is that it will not be possible for an individual to grant a statutory pledge over low-value, but essential items, such as clothing or furniture.

See paragraphs 19.50 to 19.55 of the Report.

Restriction on freedom to deal with property encumbered by statutory pledge

53 Restriction on freedom to deal with property encumbered by statutory pledge

(1) If the provider of a statutory pledge transfers the encumbered property (or any part of that property) to a third party other than with the consent mentioned in subsection (2), the transferred property remains encumbered by the pledge.

(2) The consent—

(a) is the written consent of the secured creditor—

(i) to the particular transfer, and

(ii) to the property in question being transferred unencumbered by the pledge, and

(b) does not include consent granted more than 14 days before the particular transfer.

(3) Whether to grant or withhold the consent mentioned in subsection (2) must be at the discretion of the secured creditor.

(4) The statutory pledge is extinguished if the secured creditor acquiesces, expressly or impliedly, in the provider's transfer of the encumbered property (or any part of that property) to the third party other than with the consent mentioned in subsection (2).

(5) The Scottish Ministers may by regulations—

(a) amend—

(i) any paragraph of subsection (2) (including any paragraph added to that subsection by virtue of sub-paragraph (ii)), or

(ii) that subsection by adding paragraphs which specify further descriptions of consent by reference to which subsection (1) is to apply, or

(b) amend subsection (3) by specifying further matters relevant to the granting or withholding of consent.

(6) This section is subject to sections 54 to 57.

NOTE

The creation of a statutory pledge will in nearly all cases be the result of the registration of the pledge in the Register of Statutory Pledges. The effect is that the provider of the pledge will usually keep possession of the encumbered property.

This section therefore gives statutory effect to a general principle of the law of rights in security, by providing that the statutory pledge will continue to encumber the property if it is transferred without explicit written consent by the secured creditor to the particular transfer.

The secured creditor will not be able to agree in advance that the provider is free to deal with the encumbered property, as that would enable the pledge to operate in the same manner as a floating charge.

Subsection (2) sets out that the consent of the secured creditor must be in writing, and relate to the particular transfer. Thus the consent cannot be to a transfer to any unnamed person, or to a class of persons. It must be a consent to a transfer first to a specific person, and second to that person taking the property unencumbered by the pledge.

Subsection (2) also requires that the consent must be given not more than 14 days before the transfer.

Subsection (3) sets out that the decision on whether or not to give consent must be at the discretion of the secured creditor. Thus a contractual provision under which the secured creditor must consent to any or all disposals would be ineffective.

For subsections (2) and (3), see paragraphs 20.34 to 20.36 and 20.45 of the Report.

Subsection (4) is an anti-avoidance provision, given that section 54 protects acquirers in good faith in the ordinary course of a business. A statutory pledge could become tantamount to a floating charge if the secured creditor acquiesces in the provider dealing with property without consent. If this does happen, the effect of this subsection is to extinguish the statutory pledge. See paragraphs 20.52 and 20.53 of the Report.

Subsection (5) gives the Scottish Ministers power to amend the consent provisions. This would for example enable Ministers to take account of possible future developments under English law, in relation for example to the fixed/floating characterisation of charges in an insolvency.

Subsection (6) makes it clear that the provision is subject to sections 54 to 57 which protect good faith acquirers in certain circumstances.

This section does not apply to possessory (common law) pledge, as the fact that the secured creditor holds the property limits the provider's ability to deal freely with the property.

See in general paragraphs 20.34 to 20.45 of the Report.

Acquisition of property unencumbered by a statutory pledge

54 Acquisition in good faith in ordinary course of business

(1) A purchaser of corporeal property which is encumbered property acquires it unencumbered by the statutory pledge, despite the consent mentioned in section 53(2) not having been obtained, if—

(a) the person from whom the property is acquired is acting in the ordinary course of that person's business, and

(b) at the time of acquisition, the purchaser is in good faith.

(2) For the purposes of subsection (1)(b), a purchaser is not to be taken to be other than in good faith by reason only of the statutory pledge having been registered.

(3) This section is subject to sections 55 and 56.

NOTE

Sections 54 to 57 provide for the circumstances in which a person who acquires corporeal property in good faith will acquire the property unencumbered by the statutory pledge, despite the consent mentioned in section 53(2) of the Bill not having been obtained.

It is not likely to be efficient to grant a statutory pledge over stock-in-trade given that the secured creditor must expressly consent under section 53 of the Bill to each intended transfer. Even so, encumbered property may become part of the inventory of a business. For example, Alistair might grant a statutory pledge over his piano to a bank, and then subsequently sell the instrument to a music shop. A good faith purchaser from the shop should be protected.

Subsection (1) sets out that encumbered property transferred without the consent of the secured creditor will be acquired unencumbered by a statutory pledge if two requirements are met.

First, the transferor must have been acting in the ordinary course of that person's business. For example, a motor dealer which only sells vehicles, would not on the face of it be acting in the ordinary course of business if it sold its office furniture.

Second, the acquirer must be in good faith at the time of the acquisition. The acquirer will not be protected if the acquirer knows that the property is subject to a statutory pledge.

Subsection (2) makes it clear that the acquirer is not to be deemed to have constructive knowledge of a statutory pledge for the purposes of this section merely because it is registered.

The person who acquires the property may benefit from other measures, in particular if it is acquired in good faith for personal or related purposes (see section 55 of the Bill), or the property is a motor vehicle (see section 56 of the Bill).

See paragraphs 24.23 and 24.24 of the Report.

55 Acquisition in good faith for personal, domestic or household purposes

(1) An individual who acquires corporeal property which is encumbered property acquires it unencumbered by the statutory pledge, despite the consent mentioned in section 53(2) not having been obtained, if—

(a) the value of all that is so acquired does not, as at the time of acquisition, exceed such amount (if any) as may be prescribed for the purposes of this subsection,

(b) at the time of acquisition, the acquirer is in good faith,

(c) the acquirer gives value for the property acquired, and

(d) the property is wholly or mainly acquired for personal, domestic or household purposes.

(2) This section does not apply in respect of the acquisition of encumbered property which consists of a motor vehicle.

(3) For the purposes of subsection (1)(b), an acquirer is not to be taken to be other than in good faith by reason only of the statutory pledge having been registered.

(4) In subsection (2), "motor vehicle" has the same meaning as in section 56.

NOTE

This section protects an individual who acquires corporeal property of limited value for private or related purposes.

Subsection (1) sets out that an individual who acquires encumbered property without the consent of the secured creditor having been obtained will acquire the property unencumbered if four conditions are met:

(a) The value of the property at the time of acquisition must not exceed an amount to be specified by the Scottish Ministers in regulations,

(b) The acquirer must be in good faith,

(c) The person must give value for the property acquired, normally adequate monetary value (i.e. payment of a purchase price), but also by means say of exchanging other property, and

(d) The property must be wholly or mainly acquired for personal, domestic or household purposes (business purchasers are not protected).

The effect of applying the protection at the time of acquisition is to make it easier for the individual to prove the value of the asset, and therefore that the pledge is not effective, than would be the case if any other time was fixed for that purpose.

Subsections (2) and (4) have the effect of excluding motor vehicles from the scope of this section, because these are dealt with by section 56 of the Bill.

Subsection (3) makes it clear that the acquirer is not to be deemed to have constructive knowledge of a statutory pledge for the purposes of this section merely because it is registered. It follows that the individual does not need to search the Register of Statutory Pledges before acquiring the property.

See paragraphs 24.25 to 24.30 of the Report.

56 Acquisition in good faith of motor vehicles

(1) Subsections (2) to (4) apply where—

(a) there is a sale agreement (or conditional sale agreement) or a hire-purchase agreement in respect of a motor vehicle,

(b) the motor vehicle is encumbered property,

(c) the purchaser or hirer is, at the time of entering into the agreement, in good faith, and

(d) at that time the purchaser or hirer is not a person carrying on a business described in section 29(2) of the Hire-Purchase Act 1964.

(2) On the motor vehicle being transferred to the purchaser or hirer in accordance with the agreement, that person acquires it unencumbered by the statutory pledge despite the consent mentioned in section 53(2) not having been obtained.

(3) And the statutory pledge is not to be enforced against the motor vehicle—

(a) while the agreement is extant, and

(b) before the motor vehicle is transferred to the purchaser or hirer in accordance with the agreement.

(4) But if the transferor is, at the time the agreement is entered into, a person carrying on a business described in section 29(2) of the Hire-Purchase Act 1964, the secured creditor is entitled to receive from the transferor the lesser of—

(a) the amount outstanding in respect of the secured obligation, and

(b) the amount received, or to be received, by the transferor in respect of the acquisition.

(5) For the purposes of subsection (1)(c), a purchaser or hirer is not to be taken to be other than in good faith by reason only of the statutory pledge having been registered.

(6) In this section, "conditional sale agreement", "hire-purchase agreement" and "motor vehicle" have the meanings given to those expressions by section 29(1) of the Hire-Purchase Act 1964.

(7) The Scottish Ministers may by regulations specify—

(a) motor vehicles, or

(b) classes of motor vehicle,

to which subsections (1) to (6) are not to apply.

NOTE

This section protects any person who acquires a motor vehicle that is encumbered property.

It is similar in effect to the measures in section 27 of the Hire-Purchase Act 1964 in respect of motor vehicles hired under a hire-purchase contract, or purchased under a conditional sale agreement.

Example D Ltd supplies a motor vehicle to Barry under a hire-purchase agreement with a three-year duration. Barry will not become the owner until he makes the final payment at the end of the three years. But after six months Barry sells the vehicle to Charlotte, who believes that Barry is the owner. Under section 27 of

the 1964 Act, Charlotte will become owner of the vehicle if she is in good faith and is a private purchaser.

This section achieves the same result where Barry is the owner of the vehicle, but grants a statutory pledge over it. Charlotte would take the vehicle unencumbered by the pledge if she is a good faith private purchaser from Barry.

The term "motor vehicle" is defined in section 29 of the 1964 Act as "any mechanically propelled vehicle intended or adapted for use on roads", and that definition is adopted for the purposes of this section.

Subsection (1) sets out four conditions which must be met if the encumbered property is to be acquired unencumbered, despite the consent of the secured creditor to the transfer not having been obtained.

The purchaser or acquirer must be in good faith, but subsection (5) makes it clear that the purchaser or acquirer is not to be regarded as not being in good faith only because the pledge is registered.

The hirer or purchaser of the encumbered property cannot be carrying on a business described in section 29(2) of the 1964 Act, namely a business which consists of:

(a) purchasing motor vehicles for the purpose of offering or exposing them for sale, or

(b) providing finance for purchasing motor vehicles for the purpose of hiring them under hire-purchase agreements or selling them under conditional sale agreements.

Subsection (3) protects the purchaser or hirer by preventing enforcement of the statutory pledge prior to the property being transferred in implementation of an earlier hire or sale agreement.

Subsection (4) entitles the secured creditor to a limited right of compensation against a motor dealer who transfers a vehicle that is unencumbered by the pledge.

Example John grants a statutory pledge over his car to the Ayr bank. He then sells the car to a motor dealer without the consent of the Bank. The motor dealer is not protected by subsection (2) because it should have made a search in the Register of Statutory Pledges against John and/or the car. But if the motor dealer then sells the car to a private purchaser who is protected then the Bank is entitled to be compensated by the dealer.

Subsection (7) provides for the Scottish Ministers to be able to exclude by regulations certain classes of vehicle from the application of this section.

Example The Driver and Vehicle Licensing Agency requires UK registered vehicles to have a vehicle identification number (VIN). If RSP Rules make it compulsory for an entry in the RSP to include the VIN, making it easier to check whether a particular vehicle is subject to a pledge, then Ministers might consider that the protection should not apply (say) to commercial vehicles.

See paragraphs 24.31 to 24.43 of the Report.

57 Acquisition of certain financial instruments in ordinary course of trading

(1) Subsection (2) applies where—

(a) a person, in the ordinary course of trading on a specified financial market, acquires a financial instrument of a specified kind, and

(b) that financial instrument is encumbered property.

(2) The person acquires the instrument unencumbered by the statutory pledge, despite the consent mentioned in section 53(2) not having been obtained, provided that—

(a) at the time of acquisition the person does not know of the statutory pledge, and

(b) the acquisition takes place in accordance with the rules of the specified financial market.

(3) In subsections (1)(a) and (2)(b), "specified" means specified, for the purposes of those provisions, by the Scottish Ministers by regulations.

(4) Regulations under subsection (3) may specify different markets, or descriptions of market, in relation to different kinds of financial instrument.

NOTE

This section enables the Scottish Ministers by regulations to specify certain types of financial instruments and markets in respect of which a good faith acquirer for value, in the ordinary course of trading on the specified market, will acquire an instrument that is encumbered property free from the statutory pledge.

A financial instrument for the purposes of this section is an instrument as defined in section 116(1) of the Bill, which provides that the term is to be construed in accordance with the definition in regulation 3 of the Financial Collateral Arrangements (No. 2) Regulations 2003 (S.I. 2003/3226). The definition is wide and includes shares in companies, securities equivalent to shares, and bonds tradeable on the capital market.

Subsection (2) sets out the circumstances in which the instrument would be acquired unencumbered by the pledge. They are that at the time of acquisition the acquirer does not know about the pledge, and that the acquisition takes place under the rules of the specified market.

There is therefore no requirement for the acquirer to be in good faith, or for the acquirer to give value. The effect is that this section sets a high threshold for any challenge by the secured creditor of an applicable transaction, in order to protect the interests of the person acquiring the instrument.

See paragraphs 24.44 to 24.48 of the Report.

Occupancy and other rights in matrimonial or family home following grant of statutory pledge

58 Occupancy and other rights in matrimonial or family home following grant of statutory pledge

(1) The Matrimonial Homes (Family Protection) (Scotland) Act 1981 (in this section referred to as "the 1981 Act") and the Civil Partnership Act 2004 (in this section referred to as "the 2004 Act") are amended in accordance with this section.

(2) Section 2 of the 1981 Act and section 102 of the 2004 Act are each amended in accordance with subsection (3).

(3) After subsection (8) there is inserted—

"(8A) In subsection (1)(a), "secured loan" includes secured obligation.

(8B) And in subsection (8A), "secured obligation" is to be construed in accordance with section 44(1) of the Moveable Transactions (Scotland) Act 2017.".

(4) Section 3 of the 1981 Act and section 103 of the 2004 Act are each amended in accordance with subsections (5) and (6).

(5) At the end of subsection (2) there is added "or the rights of any secured creditor in relation to the non-performance of a secured obligation".

(6) After subsection (2) there is inserted—

"(2A) In subsection (2), "secured creditor" has the meaning given to that expression by section 43(5)(a) of the Moveable Transactions (Scotland) Act 2017 and "secured obligation" is to be construed in accordance with section 44(1) of that Act.".

(7) Section 6(2) of the 1981 Act and section 106(2) of the 2004 Act are each amended in accordance with subsection (8).

(8) In the definition of "dealing", after the words "heritable security" there is inserted ", the grant of a statutory pledge".

(9) In section 8 of the 1981 Act, after subsection (2B) there is inserted—

"(2C) For the purposes of subsection (2A) above, the time of granting a security, in the case of a statutory pledge is—

(a) subject to paragraph (b), the date of delivery of the constitutive document of the statutory pledge,

(b) where the statutory pledge is granted in an amendment document, the date of delivery of that document.".

(10) In section 108 of the 2004 Act, after subsection (4) there is inserted—

"(5) For the purposes of subsection (3), the time of granting a security, in the case of a statutory pledge, is—

(a) subject to paragraph (b), the date of delivery of the constitutive document of the statutory pledge,

(b) where the statutory pledge is granted in an amendment document, the date of delivery of that document.".

(11) The title of section 8 of the 1981 Act becomes—

"**Interests of creditors**".

(12) The title of section 108 of the 2004 Act becomes—

"**Interests of creditors**".

NOTE

The Matrimonial Homes (Family Protection) (Scotland) Act 1981 gives non-owning ("unentitled") spouses occupancy rights in their matrimonial home, and in some circumstances the right to use furniture and plenishings in the home.

Section 22 of the 1981 Act defines "matrimonial home" to include a caravan or houseboat. It defines "furniture and plenishings" to mean any article in the home that is reasonably necessary to enable the home to be used as a family residence. Either type of moveable corporeal property as so defined could be encumbered property for the purposes of a statutory pledge.

The Civil Partnership Act 2004 makes the equivalent provision for civil partners as the 1981 Act does for spouses. Section 1 of the 2004 Act sets out that a civil partnership is a relationship between two people of the same sex which is formed when they register as civil partners under that Act.

In both cases, the measures in those Acts apply where one spouse or partner is entitled (or permitted by a third party) to occupy the home, and the other spouse or partner is not.

The effect of subsections (2) to (3) is that, subject to sections 2 and 102 respectively of the 1981 and 2004 Acts, an order granting a spouse or civil partner the possession or use of furniture or plenishings shall not prejudice the rights of any secured creditor in relation to the non-performance of an obligation secured by a statutory pledge. Sections 2 and 102 of those Acts confer ancillary and consequential rights on non-entitled spouses and partners, including the right to make any payment due by the entitled spouse or partner in respect of a secured obligation.

Sections 6 and 106 respectively of the 1981 and 2004 Acts provide that the continued exercise of the rights conferred on a spouse or partner by those Acts shall not be prejudiced by a dealing of the entitled spouse or partner relating to the home. The effect of subsections (4) and (5) is that a dealing will for that purpose include the grant of a statutory pledge over a moveable home, such as a caravan or houseboat.

Sections 8 and 108 respectively of the 1981 and 2004 Acts provide that the rights of a third party with an interest in the home as a creditor under a secured loan shall not be prejudiced by reason only of the rights of a non-entitled spouse or partner under those Acts, provided that in each case the creditor obtains either:

(a) a declaration from the entitled spouse that there are no occupancy rights, or

(b) a consent to the granting of the security by the non-entitled spouse.

The effect of subsections (7) to (10) is to provide for the application of those rules to the grant of a statutory pledge over a moveable home.

See paragraphs 27.55 to 27.58, and 27.64 to 27.67, of the Report.

Assignation, amendment, restriction or extinction of statutory pledge

59 Assignation of statutory pledge

(1) Except in so far as the provider and the secured creditor otherwise agree, a statutory pledge may be (and subject to subsection (3) may only be) assigned by means of a document executed or authenticated by the secured creditor.

(2) Subject to the provisions of that document, the assignation conveys to the assignee entitlement to the benefit of any notice served, or enforcement procedure commenced, by the assignor in respect of the statutory pledge before assignation (to the effect that the assignee may proceed as if the assignee served that notice or commenced those procedures).

(3) A statutory pledge which has been created under section 50(2)(a) but has not been registered, may be assigned by means of an evidenced agreement between the collateral-taker and the assignee.

NOTE

This section confirms that a statutory pledge may be assigned by means of a document duly executed or authenticated by the secured creditor (with an exception in subsection (3) in the case of an unregistered statutory pledge over a financial instrument).

A pledge is a security rather than a claim, so Part 1 of the Bill does not apply to the assignation of a pledge.

The effect is that it is not competent to register an assignation of a pledge in the new Register of Assignations. The pledge will therefore only transfer if the other requirements of the general law on assignation of rights are met, including where required delivery of the document to the assignee. It would however be possible if desired to correct the RSP to show the assignee as the secured creditor (see sections 100 and 101 of the Bill)

Subsection (2) makes it clear that a statutory pledge which is being enforced can be assigned by the secured creditor, and that the assignee can continue with the enforcement rather than having to re-commence the enforcement procedure or re-serve any notice.

See paragraphs 23.41 to 23.44, and (for subsection (3)) 37.6, of the Report.

60 Amendment of statutory pledge

(1) Subject to subsections (5) and (8), a statutory pledge—

(a) may be amended, and

(b) subject to section 61(1)(a), may only be amended,

by means of a document (in this Act referred to as an "amendment document") executed or authenticated by the secured creditor and the provider.

(2) An amendment document which relates to the addition of property to the encumbered property must identify the property to be added.

(3) The property so identified may either be property of, or property to be acquired by, the provider.

(4) Without prejudice to section 52(2), if the property to be added consists of more than one item the amendment document need not identify each item separately provided that the document identifies the items in terms of their constituting an identifiable class.

(5) An amendment document which relates only to the addition of property to the encumbered property need not be executed or authenticated by the secured creditor.

(6) Subsection (7) applies—

(a) where—

(i) the extent of the secured obligation is determinable from the terms alone of the entry for it in the statutory pledges record, and

(ii) an amendment document relates to increasing that extent, or

(b) where an amendment document relates to the addition of property to the encumbered property.

(7) Subject to section 96, the statutory pledge is amended only on registration of the amendment.

(8) Where a statutory pledge has been created under section 50(2)(a) but has not been registered, it may be amended by means of an evidenced agreement between the collateral-taker and the provider.

NOTE

This section provides for the amendment of a statutory pledge by an amendment document (as defined in this section and in section 116(1) of the Bill).

Subsection (1) provides that a statutory pledge may only be amended by an amendment document executed or authenticated by the secured creditor and the provider, subject to three exceptions.

The first exception is that the restriction of a pledge to only part of the encumbered property may be by means of a written statement by the secured creditor (for which see sections 61(1) and 118(2) of the Bill).

The second exception is that an amendment document that only adds property to the encumbered property need not be executed by the secured creditor (as is the case with the constitutive document).

The third exception is that an unregistered statutory pledge over a financial instrument may be amended by an evidenced agreement between the provider and the secured creditor.

Added property must be identified in the amendment document and may, as in the case of the constitutive document for a statutory pledge, be property to be acquired by the provider.

Subsections (6) and (7) have the effect that an amendment document that relates to the addition of property to the encumbered property, or to variation that increases the extent of the secured obligation where that is determinable from the statutory pledges record, is amended only on registration of the amendment document (for which see sections 92(1) and 96 of the Bill).

See paragraphs 23.33 to 23.40, and (for subsection (8)) 37.6, of the Report.

61 Restriction or discharge of statutory pledge

(1) A statutory pledge may, by means of a written statement by the secured creditor, be—

(a) restricted to only part of the encumbered property, or

(b) discharged.

(2) Subsection (1) does not apply in relation to a statutory pledge which—

(a) has been created under section 50(2)(a), but

(b) has not been registered.

NOTE

Subsection (1) provides for the secured creditor to be able to either restrict or discharge a statutory pledge by way of a written statement.

Subsection (2) excludes unregistered statutory pledges over financial instruments created under section 50(2)(a) from the scope of this section (but see section 62 in that respect).

See paragraphs 23.49 to 23.54 of the Report.

62 Restriction or extinction of statutory pledge created under section 50(2)(a)

(1) Subject to the provisions of this section, a statutory pledge created under section 50(2)(a)—

(a) is extinguished in relation to the financial instrument over which the pledge is created on the financial instrument ceasing to be in the possession, or under the control—

(i) of the collateral-taker, or

(ii) of a person authorised to act on behalf of the collateral-taker, and

(b) may be—

(i) restricted to only part of the encumbered property, or

(ii) discharged,

by means of an evidenced statement by or on behalf of the collateral-taker.

(2) Subsection (1) is to be construed as one with regulation 3 of the Financial Collateral Arrangements (No. 2) Regulations 2003 (S.I. 2003/3226).

NOTE

This section provides for the restriction or extinction of a statutory pledge over a financial instrument which has not been registered in the Register of Statutory Pledges.

It has the effect that the pledge is extinguished by the secured creditor (collateral-taker) giving up possession or control of the instrument, and may be restricted or discharged by means of an evidenced statement by the collateral-taker (for which see in addition section 63 of the Bill).

See paragraphs 37.8 to 37.10 of the Report.

63 Further provision as regards evidenced agreements and evidenced statements

Without prejudice to the generality of sections 59(3), 60(8) and 62(1)(b), for the purposes of those provisions an agreement, or as the case may be a statement, may be evidenced—

(a) in writing transcribed by electronic or other means in a durable medium, or

(b) in sounds recorded in such a medium.

NOTE

This section ensures that the use of evidenced agreements and evidenced statements for the purposes of sections 59 to 62 of the Bill will comply with the requirements of the Financial Collateral Arrangements (No. 2) Regulations 2003 (S.I. 2003/3226). For example, a telephone recording of a conversation may suffice to evidence an agreement to restrict a statutory pledge in respect of a financial instrument.

See paragraphs 37.6 to 37.10 of the Report.

Ranking of pledges etc.

64 Ranking

(1) Subject to the provisions of this section or of any other enactment, the priority in ranking of—

(a) any two pledges, or

(b) a pledge and a right in security other than a pledge,

is determined according to their creation, the earlier created having priority over the later.

(2) Subsection (3) applies where a provider grants, whether by means of a constitutive document or of an amendment document, two or more statutory pledges over property which, as at the time the pledges are granted, is not the property of the provider.

(3) The priority in ranking of any two of the pledges is determined, if they are pledges created as mentioned in section 48 or 49, according to the dates on which and times at which they are registered, the earlier registered having priority over the later.

(4) Where property is subject both to a pledge and to a security arising by operation of law, the security arising by operation of law has priority over the pledge.

(5) The priority in ranking of a pledge is the same irrespective of whether the secured obligation is an obligation owed or is an obligation which will or may become owed.

(6) As between—

(a) any two pledges, the secured creditors, or

(b) a pledge and a right in security other than a pledge, the secured creditor and the holder of that other right,

may set out in a written agreement that there is no priority in ranking or that any priority in ranking is determined in a way other than would be the case in the absence of such an agreement.

(7) An agreement under subsection (6)—

(a) has effect only as between the parties to it and their successors, and

(b) is not registrable.

NOTE

This section provides for the priority of payment of secured obligations in a competition between creditors, and applies to both possessory (common law) and statutory pledges.

Subsection (1) sets out the general rule that a pledge will rank against another security according to when the right is created, and is declaratory of the fundamental principle of property law *prior tempore potior jure* (earlier by time stronger by right).

Example — Patrick grants a statutory pledge over his painting to Quentin on day one. On day two, Quentin registers the pledge in the Register of Statutory Pledges. On day three Patrick creates a possessory pledge over the same painting by delivering it to Robert. The statutory pledge ranks before the possessory pledge because the former was created first.

Subsection (4) regulates the ranking of pledges and of rights in security arising by operation of law (such as the right of a repairer to retain property submitted for repair as security for payment of the bill) so that the right in security has priority. This mirrors the rule between such rights in security and floating charges, as set out in section 464(2) of the Companies Act 1985.

Subsection (5) gives a pledge priority for the entirety of the sums secured, both current and future. It follows that there is no procedure under which a party can limit the priority of the secured creditor in a higher ranking pledge by serving a notice to that effect on the creditor (as is the case for standard securities over land under section 13 of the Conveyancing and Feudal Reform (Scotland) Act 1970)).

The effect is that a party seeking a higher ranking security than is otherwise available for sums not yet due under an earlier pledge will have to negotiate a ranking agreement with the creditor in that pledge.

Subsections (6) and (7) provide for it to be possible to have a ranking agreement in respect of a pledge and another security right (including another pledge), but it needs to be in writing. Any such agreement will only have contractual effect, and cannot be registered in the Register of Statutory Pledges.

See Chapter 26 of the Report generally, and in particular paragraphs 26.3 to 26.20, 26.27 to 26.30, and 26.35 to 26.39 of the Report.

65 Amendment of Companies Act 1985 and of Insolvency Act 1986

Both in section 486(1) of the Companies Act 1985 and in section 70(1) of the Insolvency Act 1986, in the definition of "fixed security"—

(a) the words from "a heritable security" to "1970" become paragraph (a) of the definition, and

(b) after that paragraph insert—

"; or

(b) a statutory pledge ("statutory pledge" having the meaning given to that expression by section 43(4) of the Moveable Transactions (Scotland) Act 2017);".

NOTE

This section amends the Companies Act 1985 and the Insolvency Act 1986 to give effect for statutory pledges to the general rule that a real right in security (broadly, a 'fixed charge' for insolvency purposes) will, if created prior to the attachment of a floating charge, rank above the floating charge.

It does so in each case by amending the relevant definitions of "fixed security" in those Acts, with the effect that a fixed security includes a statutory pledge.

See paragraphs 20.15 to 20.26 and 26.21 to 26.23 of the Report.

66 Effect of diligence on pledge

(1) Subsection (2) applies where diligence is executed in respect of property all or any part of which is encumbered by a pledge.

(2) The pledge has, in respect of the property or as the case may be in respect of the part, priority in ranking over the diligence except in relation to any part of the secured obligation which consists of a sum—

(a) advanced after execution of the diligence, and

(b) not required to be advanced by—

(i) a contractual agreement, or

(ii) an undertaking,

entered into before execution of the diligence.

(3) Subsection (4) applies where a pledge is created over property in respect of all or any part of which diligence has been executed.

(4) The diligence has, in respect of the property or as the case may be in respect of the part, priority in ranking over the pledge.

NOTE

This section governs the priority of a pledge as regards a diligence executed against the encumbered property. The basic rule is *prior tempore potior jure* (earlier by time stronger by right). If the diligence is executed first it has priority, and if the statutory pledge is created first it prevails.

Subsection (2) provides for a special rule relating to further voluntary advances made by the secured creditor, and has the effect that an advance made after the diligence is executed does not have priority over the sum attached by the diligence unless there is a prior contractual obligation or undertaking to make the advance.

Example — Acme Ltd grants a statutory pledge over machinery for all sums due and become due to the Oban Bank, and the Bank advances £20,000 in reliance on the pledge. Louise, an unsecured creditor of Acme Ltd, then attaches the machinery for a £5,000 debt. The next day the Bank advances another £8,000 to Acme Ltd. The Bank's priority over Louise in respect of the value of the pledged property is limited to the £20,000, unless it was contractually bound to lend the further £8,000.

See paragraphs 26.31 to 26.34 of the Report.

Enforcement of pledge

67 The expression "pledge" in sections 68 to 82

In sections 68 to 82 the expression "pledge" does not include a pledge as defined in section 189(1) of the Consumer Credit Act 1974 (that is to say, does not include a pawnee's rights over an article taken in pawn).

NOTE

Sections 68 to 82 set out a statutory framework for the enforcement of both possessory and statutory pledges.

This section provides that the expression "pledge" for the purposes of those sections does not include a pledge as defined in section 189(1) of the Consumer Credit Act 1974. The effect is that a 1974 Act pledge (described in that Act as a 'pawn') falls to be enforced under the enforcement regime in respect of loans by pawnbrokers in that Act.

See paragraphs 27.14 to 27.17 of the Report.

68 Enforcement of pledge: general

(1) A pledge is enforceable in no other way than in accordance with the provisions of this Part.

(2) A pledge may be enforced—

(a) subject to any such agreement as is mentioned in paragraph (b), where there has been a failure to perform the secured obligation, or

(b) in such circumstances as are agreed between the provider and the secured creditor.

(3) Any agreement under subsection (2)(b) must be set out in writing.

(4) In enforcing a pledge a secured creditor must conform with reasonable standards of commercial practice.

(5) Subsection (2) is subject to sections 69 and 70.

NOTE

This section sets out, as a general rule, that a pledge cannot be enforced using a method not provided for by the Bill.

Example — Barry lends David £1,000, and in exchange David grants a statutory pledge over a vintage car worth £100,000. The Bill does not permit the forfeiture of encumbered property, and it is therefore unlawful for Barry to require in the event of a default that the car is forfeited to him so that he receives a windfall worth £99,000.

Subsections (2) and (3) have the effect that a pledge may be enforced in any lawful manner on default, or in such circumstances are as agreed in writing by the provider and the secured creditor. It is influenced by the DCFR IX.–1:201(5).

Subsection (4) requires the secured creditor to conform to reasonable standards of commercial practice, and is influenced by the DCFR IX.–7:103(4). Similar provision can be found in regulation 24 of the International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015 (S.I. 2015/912). See in general paragraphs 27.32 to 27.36 of the Report.

What is unreasonable for the purposes of subsection (4) will differ from case to case, but might include taking an excessively long period to complete an enforcement procedure.

Subsection (4) does not however specify to whom is owed a duty to conform to reasonable standards, and so the general law will apply. The duty might for example be owed to any of the provider, the debtor (if different), another creditor, or an office-holder such as the liquidator of a limited company.

See also the analogous duties in sections 73(2), 75(2) and 76(2) on the enforcing creditor to obtain the best reasonably attainable value where encumbered property is sold, let or licensed.

See paragraphs 27.18 to 27.28 and 27.32 to 27.36 of the Report, and – as regards possessory pledge – paragraphs 25.18 to 25.22 of the Report.

69 Pledge Enforcement Notice

(1) Before taking any other steps to enforce a pledge the secured creditor must serve—

(a) on the provider,

(b) on the holder of any other right in security over the encumbered property, or over any part of that property,

(c) on any creditor who has executed diligence against the encumbered property, or against any part of that property,

(d) on any person who has statutory duties in relation to the provider's estate and is prescribed under this paragraph, and

(e) in the case of a statutory pledge, on any occupier of the encumbered property, or of any part of that property, (whether or not that occupier is also the provider),

a notice in, or as nearly as may be in, a form prescribed for the purposes of this subsection.

(2) Except that—

(a) paragraph (b) of subsection (1) is to be disregarded if the secured creditor does not know, and cannot reasonably be expected to know, of the right in security mentioned in that paragraph, and

(b) paragraph (c) of that subsection is to be disregarded if the secured creditor does not know, and cannot reasonably be expected to know, of the diligence executed as mentioned in that paragraph.

(3) Different forms may be prescribed by virtue of subsection (1) for different categories of provider or occupier.

(4) A notice served under subsection (1) is to be known as a "Pledge Enforcement Notice".

(5) If, by virtue of subsection (1)(e) of section 87 of the Consumer Credit Act 1974, a default notice must be served on the provider, the requirements of that section and of section 88 of that Act must be satisfied before a Pledge Enforcement Notice is served.

(6) In subsection (5), "default notice" has the meaning given to that expression by section 87(1) of that Act.

NOTE

This section provides for a pledge enforcement notice, to be served before any enforcement action by the secured creditor on the provider and other interested persons (if any). A notice would for example require to be served on any person occupying a motorhome or house boat encumbered by a statutory pledge.

The Scottish Ministers are able by regulations to prescribe different forms of notice for different categories of provider or occupier (see section 118(1) for the definition of "prescribed"). For example, a form for individual providers might contain information on how to obtain legal advice, and the information that the creditor will need to obtain a court order before the pledge can be enforced.

The Scottish Ministers are also able by regulations to prescribe that notice must be given to a person who has statutory duties in relation to the provider's property, as is the case for example in an insolvency.

Subsections (5) and (6) make it clear that the requirement to serve a pledge enforcement notice is subject to sections 87 and 88 of the Consumer Credit Act 1974, which requires a 14-day default notice to be served before the enforcement of any right in security which is subject to that Act.

If the 1974 Act applies then the default notice for the purposes of that Act will have to be served 14 days before the pledge enforcement notice can be served.

See paragraphs 27.37 to 27.45 and 27.59 to 27.63 of the Report.

70 Whether court order required for enforcement of pledge

(1) In a case where the provider of a pledge is an individual, a court order is required for enforcing the pledge unless—

(a) after the pledge becomes enforceable by virtue of section 68(2), the provider agrees in writing to its being enforced without such an order, or

(b) the provider being a sole trader, enforcement is against property used wholly or mainly for the purposes of the provider's business.

(2) And a court order is required for enforcing a statutory pledge in respect of property which is the sole or main residence of an individual unless, after the pledge becomes enforceable by virtue of section 68(2)—

(a) the secured creditor,

(b) the provider, and

(c) (in any case where the individual is not the provider) the individual,

agree otherwise in writing.

(3) Other than is mentioned in subsection (1) or (2), a court order is not required for enforcing a pledge.

(4) The court is not to grant an order required by subsection (2) unless satisfied that enforcement is reasonable in all the circumstances of the case.

(5) Without prejudice to the generality of subsection (4), those circumstances include—

(a) the nature of, and reason for, the default by virtue of which authority to enforce is sought,

(b) whether the person in default has the ability to remedy the default within a reasonable time,

(c) whether the secured creditor has done anything to help the person in default remedy the default,

(d) where it is, or was, appropriate for the person in default to take part in a debt payment programme approved under Part 1 of the Debt Arrangement and Attachment (Scotland) Act 2002, whether that person is taking part, or has taken part, in such a programme, and

(e) whether reasonable alternative accommodation is available for (or can be expected to be available for) the individual whose sole or main residence is the property in question.

(6) Subsection (3) is subject to section 71(3) and (7) and to section 72(2) and (5).

NOTE

This section has the effect that a court order is required before a pledge is enforced against the individual, unless agreed otherwise by the individual after default. The effect is that an individual cannot agree in advance that a court order is not required.

Subsection (2) deals with property subject to a statutory pledge which is the sole or main residence of an individual, although that will be unusual as a pledge can only be granted over moveable property. A court order is required unless there is a written agreement to enforcement after default between the person in residence, the provider (if a different person) and the secured creditor.

Subsection (3) confirms that a court order is not required in other cases.

Subsection (6) sets out that subsection (3) is subject to sections 71 and 72 of the Bill, and confirms that in the case of a statutory pledge over respectively corporeal moveable property or a financial instrument a court order will be required in the circumstances set out in those sections.

See paragraphs 27.46 to 27.54 and 27.59 to 27.63 of the Report.

71 Secured creditor's right to take possession of corporeal property or to ensure it is not disposed of or used in an unauthorised way

(1) Subsections (2) to (4) apply in relation to corporeal property in respect of which a secured creditor in a statutory pledge has served a Pledge Enforcement Notice.

(2) Subject to subsection (3), the secured creditor is entitled—

(a) to take possession of the property, or

(b) to take any reasonable steps necessary to ensure, whether or not by immobilising the property, that it is not disposed of or used in an unauthorised way.

(3) The secured creditor may take such possession or such steps—

(a) with the consent—

(i) of the provider given after the pledge becomes enforceable, and

(ii) of any third party who for the time being either is in direct possession of, or has custody of, the property,

(b) through the agency of an authorised person, or

(c) personally, if authorised to do so by the court.

(4) The secured creditor is entitled, in taking possession of the property under subsection (2)(a), to remove any individual from that property (but only through such agency as is mentioned in subsection (3)(b)).

(5) Subsections (2) to (4) are subject to subsections (6) and (7).

(6) The secured creditor has no entitlement under subsections (2) to (4) if the circumstances are that the property is in the possession of a person who, in respect of the property or of any part of the property—

(a) has a right in security which has priority in ranking over, or ranks equally with, the pledge to which the Pledge Enforcement Notice relates, or

(b) has executed diligence which has priority in ranking over, or ranks equally with, that pledge.

(7) But in the circumstances mentioned in subsection (6) the secured creditor may—

(a) with the consent of the person who has the right in security over, or has executed diligence against, the property,

(b) with the consent of the court, through such agency as is mentioned in subsection (3)(b), or

(c) personally, if authorised to do so by the court,

take possession of the property or take such steps as are mentioned in subsection (2)(b).

(8) Subsection (4) applies in relation to taking possession under subsection (7) as it applies in relation to taking possession under subsection (2).

(9) In subsection (3)(b), "authorised person" means—

(a) a messenger-at-arms or sheriff officer,

(b) a person qualified to act as an insolvency practitioner, or

(c) such other person as may be prescribed for the purposes of that subsection.

(10) Paragraph (b) of subsection (9) is to be construed in accordance with section 390 of the Insolvency Act 1986.

(11) This section is subject to section 70.

NOTE

This section provides for enforcement of a statutory pledge by the secured creditor following service of a pledge enforcement notice, and where appropriate the obtaining of a court order.

It enables the secured creditor to take possession of the encumbered property from, typically, the provider.

Subsection (2)(b) also enables the creditor to take any reasonable steps necessary to ensure that the property is not disposed of or used in any unauthorised way. It is influenced by the DCFR IX.–7:202(1), and is aimed at larger assets such as machinery where it might be more convenient to sell them on site. The secured creditor may simply want to immobilise the asset, so that it cannot be removed before any planned sale.

Subsection (3) has the effect that possession may only be lawfully taken using one of three methods. First, it may be taken with the consent of the provider or holder of the property. Second, it may be taken by an authorised person for the purposes of this section, such as an insolvency practitioner. Third, it may be taken by the secured creditor personally if authorised by the court.

Subsection (4) enables the secured creditor, acting through an authorised person, to remove any individual from the encumbered property. This might be necessary where the encumbered property is, for example, a motorhome or houseboat.

Subsection (6) restricts the rights of the secured creditor under this section where the property is in the possession of an equal or higher ranking secured creditor, or a creditor who has higher or equivalently ranking diligence against the property. It should however be read with subsection (7).

Subsection (7) allows possession to be taken in those circumstances by consent, or with the authority of the court. Thus it may be that the higher ranking creditor does not wish to enforce its security. In these circumstances the lower ranking statutory pledge holder may seek consent to obtain possession of the property so that their pledge can be enforced.

Subsections (9) and (10) have the effect of defining "authorised person" for the purposes of this section, and enable the Scottish Ministers to prescribe by regulations other persons as an authorised person.

See paragraphs 27.68 to 27.79 of the Report.

72 Secured creditor's right to take possession of certificate of financial instrument

(1) Subsection (2) applies in relation to a certificated financial instrument in respect of which a secured creditor in a statutory pledge has served a Pledge Enforcement Notice.

(2) The secured creditor is entitled to take possession of the certificate of the instrument—

(a) with the consent—

(i) of the provider given after the pledge becomes enforceable, and

(ii) of any third party who for the time being either is in direct possession of, or has custody of, that certificate,

(b) through the agency of an authorised person, or

(c) personally, if authorised to do so by the court.

(3) Subsection (2) is subject to subsection (4).

(4) The secured creditor has no entitlement under subsection (2) if the certificate is for the time being in the possession of a person—

(a) who has a right in security over the instrument, being a right in security which has priority over, or ranks equally with, the pledge to which the Pledge Enforcement Notice relates, or

(b) who has executed diligence against the instrument and by virtue of that diligence has priority in ranking over, or ranks equally with, the secured creditor.

(5) But in the circumstances mentioned in subsection (4) the secured creditor may—

(a) with the consent of the person who has the right in security over, or has executed diligence against, the instrument,

(b) with the consent of the court, through such agency as is mentioned in subsection (2)(b), or

(c) personally, if authorised to do so by the court,

take possession of the certificate for the instrument.

(6) In subsection (2)(b), "authorised person" has the meaning given to that expression by subsection (9) of section 71 (as read with subsection (10) of that section).

(7) This section is subject to section 70.

NOTE

This section makes provision for the secured creditor to be able to take possession of a certificated financial instrument (see the definition of "financial instrument" in section 116(1) of the Bill).

A financial instrument is a type of incorporeal moveable property, but ownership of the instrument may be evidenced by (for example) a share certificate. The secured creditor should be able to take possession of any such certificate for the purpose of enforcing a statutory pledge over the instrument.

This section therefore provides for the taking of possession of a certificated instrument in broadly the same manner as section 71 provides for the creditor to take possession of corporeal moveable property.

This section does not however modify or restrict the rights of a collateral-taker under the Financial Collateral Arrangements (No. 2) Regulations 2003 (S.I. 2003/3226) on the occurrence of an enforcement event, as defined in regulation 3(1A) of those Regulations. See section 84 of the Bill in that respect.

See paragraphs 27.80 and 27.8 of the Report.

73 Secured creditor's entitlement to sell

(1) Where a Pledge Enforcement Notice has been served in respect of property, the secured creditor is entitled to sell all or any of that property.

(2) The secured creditor, in selling property by virtue of subsection (1), must take all reasonable steps to ensure that the price obtained is the best reasonably obtainable.

(3) Subject to subsection (4), the secured creditor is entitled to purchase all or any of the property but only—

(a) in a sale by public auction, and

(b) for a price which bears a reasonable relationship to market value.

(4) If the property is of a kind admitted to trading in a public market in which current market value is verifiable at time of purchase, the secured creditor is entitled to purchase all or any of the property but only—

(a) in that market, and

(b) for market value.

(5) Any proceeds obtained by virtue of subsection (1) are to be held in trust by the secured creditor until applied under section 82.

(6) This section is subject to section 70.

NOTE

This section sets out the standard remedy for the secured creditor following service of a pledge enforcement notice (and where appropriate the obtaining of a court order): a right to sell the property at the best reasonably attainable price.

The secured creditor will need to be able to convey the encumbered property to the purchaser, and may first require to take possession of the property under sections 71 or 72 of the Bill.

The secured creditor may purchase the encumbered property, but only in the limited circumstances set out in subsections (3) and (4).

Subsection (5) requires that the secured creditor holds the proceeds of sale in trust until they are distributed under section 82 of the Bill. It is similar in effect to section 27 of the Conveyancing and Feudal Reform (Scotland) Act 1970, which provides for the proceeds of sale under a standard security over land. A standard security is another form of subordinate real right in security.

See paragraphs 28.2 to 28.8 of the Report.

74 Sale effected by virtue of section 73(1): unencumbered acquisition

(1) Subsections (2) and (3) apply where a secured creditor sells property by virtue of section 73(1) and transfers the property to the purchaser.

(2) The purchaser acquires the property unencumbered by—

(a) the pledge, and

(b) any right in security, or any diligence, ranking equally with or postponed to the pledge.

(3) But the purchaser acquires the property unencumbered by any—

(a) right in security, or

(b) diligence,

which has priority in ranking over the pledge only if the holder of the right in security, or as the case may be the creditor who executed the diligence, consented to the sale.

NOTE

This section provides for the effect of a sale of the encumbered property on the rights of:

(a) any creditor under another security that encumbers the property, and

(b) any unsecured creditor who has attached or arrested the property in connection with enforcing a court order for payment (diligence).

It provides that the purchaser acquires the property free of the pledge that is being enforced, and of any rights in security or diligence which rank equally with or after the pledge.

It provides a separate rule for higher ranking rights in security or diligence. These continue to encumber the property unless the relevant creditor consented to the sale (as influenced by the DCFR IX.–7:213(2)).

See paragraphs 28.9 to 28.13 of the Report.

75 Secured creditor's entitlement to let

(1) A secured creditor who by virtue of section 73(1) is entitled to sell corporeal property is entitled to let all or any of that property.

(2) The secured creditor, in letting property by virtue of subsection (1), must take all reasonable steps to ensure that the income obtained is the best reasonably obtainable.

(3) Any rental income obtained by virtue of subsection (1) is to be held in trust by the secured creditor until applied under section 82.

(4) The provider and the secured creditor may agree, whether before or after the pledge becomes enforceable by virtue of section 68(2), that subsection (1) is not to apply as regards the corporeal property or some part of that property.

(5) Any such agreement must be set out in writing.

NOTE

This section has the effect that, where it is lawful to sell encumbered property under section 73 of the Bill, it is also lawful to lease the property. It is influenced by the DCFR IX.–7:207(b).

Subsections (4) and (5) provide for the parties to be able to agree in writing at any time to exclude leasing as a remedy available to the secured creditor on default. For example, the provider may wish to have sale as the sole remedy on the basis that this would pay off the secured debt more quickly (and the creditor may also favour speed).

See paragraphs 28.14 and 28.15 of the Report.

76 Secured creditor's entitlement to grant licence over intellectual property

(1) A secured creditor who by virtue of section 73(1) is entitled to sell intellectual property is entitled to grant a licence over all or any of that property (but only if and to the extent that the provider is entitled to grant such a licence).

(2) The secured creditor, in granting a licence by virtue of subsection (1), must take all reasonable steps to ensure that the income obtained is the best reasonably obtainable.

(3) Any income obtained by virtue of subsection (1) is to be held in trust by the secured creditor until applied under section 82.

(4) The provider and the secured creditor may agree, whether before or after the pledge becomes enforceable by virtue of section 68(2), that subsection (1) is not to apply as regards the intellectual property or some part of that property.

(5) Any such agreement must be set out in writing.

NOTE

A licence of intellectual property is effectively a lease of that type of property (although it is not necessarily exclusive), and this section has therefore a similar purpose and effect for such property as section 75 does for property that can be leased.

See paragraphs 28.16 to 28.18 of the Report.

77 Secured creditor's entitlement to protect, maintain and manage and to preserve the value of encumbered property

(1) A secured creditor who by virtue of section 73(1) is entitled to sell property is entitled to take reasonable steps—

(a) to protect, maintain and manage it, and

(b) to preserve its value.

(2) Without prejudice to the generality of subsection (1), the secured creditor may, by virtue of that subsection—

(a) where the property consists of, or includes, a financial instrument, exercise any voting rights in relation to the financial instrument,

(b) effect or maintain an insurance policy in relation to the property,

(c) settle any liability in relation to the property,

(d) bring, defend or continue legal proceedings in relation to the property,

(e) take such other steps as the provider, whether before or after the pledge becomes enforceable by virtue of section 68(2), has agreed may be taken by the secured creditor.

(3) Subsection (1) is without prejudice to section 71(2)(b).

NOTE

This section provides for a secured creditor entitled to sell encumbered property under section 73 to be able to take additional measures to protect *etcetera* the property as specified in the section, and to preserve its value.

See paragraphs 28.19 to 28.20 of the Report.

78 Secured creditor's right to appropriate: general

(1) Where a Pledge Enforcement Notice has been served the secured creditor is entitled, subject to subsections (2) and (3), to appropriate any or all of the encumbered property in satisfaction, in whole or in part, of the secured obligation.

(2) It is not competent to appropriate by virtue of subsection (1)—

(a) the property of an individual unless that person is a sole trader and the appropriation is of assets used wholly or mainly for the purposes of the person's business,

(b) corporeal property, or a financial instrument payable to bearer, unless that property or instrument is in the possession of the secured creditor, or

(c) property the value of which exceeds an amount which is the total of—

(i) the amount for the time being remaining due under the secured obligation, and

(ii) such expenses as have reasonably been incurred by the secured creditor in enforcing the pledge.

(3) Except that property the value of which exceeds the total mentioned in paragraph (c) of subsection (2) may be so appropriated (subject to paragraphs (a) and (b) of that subsection) provided that a sum of money equivalent to the amount by which that total is exceeded is set aside by the secured creditor and held in trust until applied under section 82.

NOTE

Sections 78 to 81 of the Bill provide the secured creditor who has served a pledge enforcement notice to be able, in specified circumstances, to appropriate the encumbered property on default by the provider.

This is not the same as forfeiture of the property, which is not permitted.

This section provides in subsection (1) for the general right to appropriate. A creditor who appropriates property becomes the owner of the property.

Subsection (2) excludes appropriation in specified cases. In particular it excludes appropriation of:

(a) Property of an individual, other than in respect of the business assets of a sole trader,

(b) Corporeal property or bearer bonds that are not possessed by the creditor (for practical reasons), and

(c) Property the value of which is greater than the amount remaining due under the secured obligation, including reasonable expenses, without reimbursing the excess.

There is the potential for abuse of a right to appropriate encumbered property, as the value of the property could greatly exceed the sum due to the secured creditor. Modern practice, as set out for example in the DCFR, recognises the need to safeguard the interests of the provider of the pledge (for which see the DCFR IX.–7:105 and 7:216).

Subsection (3) therefore provides for the secured creditor to be able to appropriate property the value of which is greater than the sum due to the creditor, but only if the creditor holds a sum representing the excess value in trust pending distribution under section 82 of the Bill.

See paragraphs 28.38 to 28.43 of the Report.

79 Appropriation where no agreement reached under section 80(1)

(1) Before exercising any right to appropriate property by virtue of section 78(1), the secured creditor must serve a notice on—

(a) the provider,

(b) the debtor in the secured obligation if a person other than the provider,

(c) the holder of any other right in security over all or part of the property,

(d) any person who has executed diligence against all or part of the property, and

(e) any person who has statutory duties in relation to the provider's estate and is prescribed under this paragraph.

(2) Except that—

(a) paragraph (c) of subsection (1) is to be disregarded if the secured creditor does not know, and cannot reasonably be expected to know, of the right in security mentioned in that paragraph, and

(b) paragraph (d) of that subsection is to be disregarded if the secured creditor does not know, and cannot reasonably be expected to know, of the diligence executed as mentioned in that paragraph.

(3) Any notice served under subsection (1) must—

(a) identify the property to be appropriated,

(b) specify—

(i) the amount for the time being remaining due under the secured obligation, and

(ii) the amount to be obtained by the appropriation, and

(c) state that, within 14 days after service of the notice, the recipient may object to the appropriation.

(4) The appropriation is not to proceed unless the amount obtained by it bears a reasonable relationship to the market value of the property appropriated.

(5) If within 14 days after receiving notice by virtue of subsection (1) a recipient, by means of a written statement to the secured creditor, objects to the appropriation—

(a) the appropriation is not to proceed, and

(b) the secured creditor must, by written statement and without delay, inform each of the other recipients of a notice under subsection (1) that the appropriation is not to proceed.

(6) Subsections (1) to (5) are to be disregarded as respects property in relation to which the provider and the secured creditor have reached agreement under section 80(1).

NOTE

Sections 79 and 80 provide respectively for appropriation without, and with, an agreement to the use of appropriation by the secured creditor as a remedy on default.

Under this section only, given that there is no agreement, the provider is entitled to object in principle to the use of appropriation in respect of the particular encumbered property.

Any appropriation must be for an amount which bears a reasonable relationship to the market value of the property. Thus machinery worth £10,000 cannot be appropriated as being worth £1,000.

Subsection (1) requires notice of the intended appropriation to be given to the parties it will affect. The provision is self-explanatory, except for sub-paragraph (e) which provides for notice to be given to a person who has statutory duties in relation to the provider's estate and is specified for that purpose by the Scottish Ministers by regulations.

Subsection (3) sets out that the notice on intended appropriation must identify the property to be appropriated, and specify both the amount owing to the secured creditor and the amount to be obtained by the appropriation.

Subsection (5) gives the parties to whom the notice is served a right to veto the appropriation, provided they do so within 14 days after receipt of the notice of the intended appropriation.

Subsection (6) disapplies this section where there is a pre-default agreement on appropriation under section 80.

See paragraphs 28.45 to 28.48 of the Report.

80 Agreement as to appropriation by virtue of section 78(1)

(1) The provider and the secured creditor may, before the pledge becomes enforceable by virtue of section 68(2), agree that the secured creditor is entitled to appropriate by virtue of section 78(1)—

(a) the encumbered property, or

(b) any part of that property.

(2) Any agreement under subsection (1) must be set out in writing.

(3) And property appropriated in accordance with that agreement—

(a) must be—

(i) a fungible asset that is traded on a specified market, being a market the prices on which are published and widely available (whether on payment of a fee or otherwise), or

(ii) if it is not such an asset so traded, property as regards which the provider and the secured creditor have, in the agreement, set out a method of readily determining a reasonable market price, and

(b) is appropriated only for the value, at the date of appropriation, of the property's market price—

(i) as so published, or

(ii) as the case may be, as so determined.

(4) Before exercising any right to appropriate property by virtue of subsection (1), the secured creditor must serve a notice on—

(a) the provider,

(b) the debtor in the secured obligation if a person other than the provider,

(c) the holder of any other right in security over all or part of the property,

(d) any person who has executed diligence against all or part of the property, and

(e) any person who has statutory duties in relation to the provider's estate and is prescribed under this paragraph.

(5) Except that—

(a) paragraph (c) of subsection (4) is to be disregarded if the secured creditor does not know, and cannot reasonably be expected to know, of the right in security mentioned in that paragraph, and

(b) paragraph (d) of that subsection is to be disregarded if the secured creditor does not know, and cannot reasonably be expected to know, of the diligence executed as mentioned in that paragraph.

(6) A notice under subsection (4) must—

(a) identify the property to be appropriated,

(b) specify—

(i) the amount for the time being remaining due under the secured obligation, and

(ii) the amount to be obtained by the appropriation, and

(c) state that, within 14 days after service of the notice, the recipient (if a person other than the provider or the debtor) may object to the appropriation.

(7) If within 14 days after receiving notice by virtue of any of paragraphs (c) to (e) of subsection (4) a recipient, by means of a written statement to the secured creditor, objects to the appropriation—

(a) the appropriation is not to proceed, and

(b) the secured creditor must, by written statement and without delay, inform each of the other recipients of a notice under subsection (4) that the appropriation is not to proceed.

(8) In subsection (3)(a)(i)—

(a) "fungible asset" means an asset of a nature to be dealt in without identifying the particular asset involved, and

(b) "specified" means specified, for the purposes of this section, by the Scottish Ministers by regulations.

(9) Regulations under subsection (8)(b) may specify different markets, or descriptions of market, in relation to different kinds of fungible asset.

NOTE

This section allows the provider and the secured creditor to agree in writing, in advance of any default in or enforcement of the secured obligation, that the creditor may subject to certain conditions appropriate the encumbered property. It is influenced by the DCFR IX.–7:105.

The provider and other parties are given notice of the intended appropriation in the same manner as for appropriation without agreement, but the provider (and debtor if a different person to the provider) is not entitled to object.

Subsection (3) has the effect that an agreement to appropriate may only have effect as respects the two types of property specified in this subsection.

The first type is property which is a fungible asset traded on a market specified by the Scottish Ministers by regulations under subsection (8)(b), being a market where prices are published and widely available. "Fungible asset" is itself defined in subsection (8)(a) with the effect that it includes property comprised of individual units which are capable of mutual substitution, for example company shares.

The second type is property which is not traded on a specified market as above, but in respect of which the agreement sets out a method of easily determining a reasonable market price. That might include for example an agreement in relation to appropriation of used cars which states that an average of the prices listed in a specified used car guide is to be used to determine the value on appropriation.

See paragraphs 28.49 to 28.55 of the Report.

81 Appropriation by virtue of section 78(1): unencumbered acquisition

(1) Subsection (2) applies where a secured creditor appropriates property by virtue of section 78(1).

(2) The secured creditor acquires the property unencumbered by any right in security or any diligence.

NOTE

This section provides that any other right in security over or diligence in respect of the encumbered property is extinguished by an appropriation by virtue of section 78 of the Bill.

Any other secured creditor or a creditor who has executed diligence will have been given notice of the intended appropriation under section 79 or 80 of the Bill, unless the creditor did not know – or could not reasonably be expected to know - of the security or diligence.

A creditor who is given notice has the right to object to the proposed appropriation under those sections.

See paragraphs 28.56 and 28.57 of the Report.

82 Application of proceeds arising from enforcement of pledge

(1) Any proceeds arising from the enforcement of a pledge are to be applied—

(a) firstly, in payment of all expenses reasonably incurred by the secured creditor in connection with the enforcement, and

(b) secondly, in payment of the amount due to—

(i) the holder of any right in security over the property from which the proceeds arose, or

(ii) any creditor who has executed diligence against that property.

(2) Any payment made by virtue of subsection (1)(b) is to be made in conformity with the ranking of the right in security or, as the case may be, of the diligence.

(3) No such payment is to be made—

(a) to the holder of a right in security which has priority in ranking over the pledge enforced, or

(b) to any creditor who has executed diligence which has such priority,

unless that holder or creditor consented to the enforcement in question.

(4) Any residue from the proceeds so arising is to be paid to the provider.

(5) Where payment falls to be made, by virtue of subsection (1)(b), to more than one person with the same ranking but the proceeds are inadequate to enable those persons to be paid in full, their payments are to abate in equal proportions.

(6) Subsections (7) to (9) apply where a question arises as to whom a payment under this section is to be made.

(7) The secured creditor must—

(a) consign the amount of the payment (so far as ascertainable) in court for the person appearing to have the best right to that payment, and

(b) lodge in court a statement of the amount consigned.

(8) A consignation made in pursuance of subsection (7)(a) operates as a payment of the amount due.

(9) A certificate of the court is sufficient evidence of that payment.

(10) Without prejudice to the generality of subsection (1)(a), the expenses mentioned in that subsection include any that may be incurred under section 71(2) or 77.

(11) The secured creditor must, as soon as reasonably practicable, present—

(a) the provider,

(b) the debtor in the secured obligation if a person other than the provider,

(c) any person who both—

(i) is mentioned in subsection (1)(b), and

(ii) has consented to the enforcement in question, and

(d) any person who has statutory duties in relation to the provider's estate and is prescribed under this paragraph,

with a written statement of how the proceeds arising from the enforcement have been applied under this section.

(12) In a case where, by virtue of—

(a) section 75(1), all or any of the property is let by the secured creditor, or

(b) section 76(1), the secured creditor grants a licence over all or any of it,

subsection (11) applies as regards any proceeds of the letting or licensing as if, for the words "as soon as reasonably practicable", there were substituted "every month after the first proceeds arising from the enforcement are received".

NOTE

This section provides for the distribution of any proceeds received by the secured creditor as a result of enforcing a possessory or statutory pledge.

It provides that the secured creditor must first pay the expenses of the enforcement (see subsection (10)), and then pay the sums due to secured creditors or creditors who have executed diligence in accordance with the priority of their claims. Any residue is paid to the provider (see in that respect paragraph (c) of the definition of "provider" in section 116(1) of the Bill).

Payments are to be abated in equal proportions where full payment is not possible.

Example — The encumbered property is sold for £100,000. There are two equal ranking rights in security. Jack is owed £200,000. Jill is owed £50,000. Jack is paid £80,000 and Jill £20,000, which is 40% of what is due to each of them.

Subsection (3), however, sets out that no payment is to be made to creditors with a higher ranking security or diligence than the pledge being enforced, unless they have consented to the enforcement. If they have not consented then their right still subsists, and that will affect the marketability of the encumbered property (see section 74(3) in that respect). It might mean, for example, that is only practicable for the secured creditor to lease the encumbered property.

Subsections (6) to (9) provide for the situation, likely to be uncommon, where it is unclear who is to be paid or a receipt for payment cannot be obtained (perhaps because a secured creditor cannot be traced). The effect is that the secured creditor must consign an amount in court for the benefit of the person who appears to have the best right to the payment.

Subsections (11) and (12) provide for statements to be made to relevant parties as to how the proceeds as a whole have been distributed. The creditor must give a statement to such persons with relevant statutory duties as are prescribed by the Scottish Ministers (see section 118(1) for the definition of "prescribed").

See paragraphs 28.21 to 28.37 of the Report.

83 Circumstances in which application must be made for removal of an entry from the statutory pledges record

(1) Subsection (2) applies where a statutory pledge which has been registered is extinguished by virtue of—

(a) the enforcement of the statutory pledge,

(b) the enforcement of another right in security over the encumbered property of the statutory pledge, or

(c) the execution of diligence against the encumbered property of the statutory pledge.

(2) The secured creditor must, as soon as reasonably practicable, make an application under section 100(1) for removal of the entry for the statutory pledge from the statutory pledges record.

NOTE

This section imposes a duty on the secured creditor in a statutory pledge to apply under section 100 of the Bill for the correction of the RSP where the pledge is extinguished by any of the enforcement of the pledge, enforcement of any other secured right, or the use of diligence.

Example — Adam grants a statutory pledge for a debt of £10,000 to Eve over machinery. Adam then grants a second ranking statutory pledge to Cain for a debt of £5,000 over the same machinery. Adam subsequently defaults on his secured obligation to Cain.

Eve consents to Cain enforcing the second pledge subject to Eve, as higher ranking creditor, being paid from the proceeds. The plant and machinery is sold for £20,000. Cain divides the proceeds so that Eve is paid £10,000, Cain keeps £5,000, and the remaining £5,000 is paid to Adam.

Eve and Cain are both subject to a duty to remove their pledge from the statutory pledges record.

See paragraph 28.58 of the Report.

84 Sections 68 to 82: saving

Nothing in sections 68 to 82 is to be taken to derogate from such rights as a secured creditor may have by virtue of Part 4 of the Financial Collateral Arrangements (No. 2) Regulations 2003 (S.I. 2003 No. 3226).

NOTE

This section applies where a statutory pledge is granted over a financial instrument for the purpose of evidencing a financial collateral arrangement, and has the effect that the enforcement provisions in the Bill are without prejudice to the rights of the secured creditor under Part 4 of the Financial Collateral Arrangements (No. 2) Regulations 2003 (S.I. 2003/3226).

See paragraphs 37.13 and 37.14 of the Report.

Liability for loss suffered by virtue of enforcement

85 Liability for loss suffered by virtue of enforcement

(1) A person (in subsection (2) referred to as "P") is entitled to be compensated by a secured creditor for loss suffered in consequence of the secured creditor's failure to comply with any obligation imposed on the secured creditor by any provision of sections 68 to 83.

(2) But the secured creditor has no liability under subsection (1)—

(a) in so far as P's loss could have been avoided had P taken measures which it would have been reasonable for P to take, or

(b) in so far as P's loss was not reasonably foreseeable.

NOTE

This section imposes liability on the secured creditor for failing in any duty imposed by the Bill on the creditor in relation to the enforcement of a possessory or statutory pledge.

Subsection (2) restricts liability in the specified cases, but does not exclude liability for non-patrimonial loss. The effect is that there may be circumstances where compensation for pain and suffering (solatium) could be claimed, for example the provider following the taking of possession of a houseboat in an unlawful manner.

See paragraphs 28.59 to 28.64 of the Report.

Service of documents for purposes of this Chapter of Part 2

86 Service of documents for purposes of this Chapter of Part 2

(1) In relation to the service of documents for the purposes of this Chapter of Part 2, the provider and the secured creditor may agree (either or both)—

(a) that the document may be served on a person by being sent to a specified address (being an address other than is mentioned in subsection (4) of section 26 of the Interpretation and Legislative Reform (Scotland) Act 2010),

(b) that service is to be by a specified method (being a method mentioned in subsection (2) of that section).

(2) The agreement need not refer expressly to that section or to any provision of that section.

(3) In subsection (1), "specified" means specified in the agreement.

(4) Any such agreement must be set out in writing.

(5) Where there is such an agreement but service cannot be effected in accordance with it, the agreement is to be disregarded in applying section 26 of that Act of 2010 for the purposes of this Chapter.

NOTE

The default rules for service of documents in or under an Act of the Scottish Parliament are set out in section 26 of the Interpretation and Legislative Reform (Scotland) Act 2010.

The section provides for the provider and the secured creditor to be able to agree in writing that service may be in accordance with this section. Thus, for example, the parties might provide that an enforcement notice may only be sent by registered delivery.

An agreement under this section could be (for example) included in the constitutive document for the statutory pledge.

Subsection (4) has the effect that where service cannot be effected in accordance with the agreement then the default rules in the 2010 Act will apply.

See paragraphs 28.65 to 28.67 of the Report.

CHAPTER 2

REGISTER OF STATUTORY PLEDGES

Register of Statutory Pledges

87 The Register of Statutory Pledges

(1) There is to be a public register known as the Register of Statutory Pledges.

(2) The Register of Statutory Pledges (in this Part referred to as "the register") is to be under the management and control of the Keeper.

(3) Subject to the provisions of this Act the register is to be in such form as the Keeper thinks fit.

(4) The Keeper is to take such steps as appear reasonable to the Keeper for protecting the register from—

(a) interference,

(b) unauthorised access, or

(c) damage.

(5) Section 110 of the Land Registration etc. (Scotland) Act 2012 (fees) applies in relation to the register as it applies in relation to any other register under the management and control of the Keeper.

NOTE

Subsection (1) establishes the new register in which statutory pledges can be registered, to be known as the Register of Statutory Pledges ("RSP"). See paragraphs 29.2 to 29.5 of the Report.

Subsection (2) provides that the RSP is to be under the management of the Keeper of the Registers of Scotland (for which see the definition in section 118(1) of the Bill). See paragraphs 29.6 to 29.8 of the Report.

Subsection (3) states that, subject to the requirements laid down by the Bill, the Keeper has discretion as to the form in which the RSP is kept. That would include keeping the RSP in electronic form.

For subsections (3) and (4), see paragraphs 29.22 to 29.23 of the Report.

The RSP, like the other registers under the Keeper's control, is an important public asset. Subsection (4) therefore provides that the Keeper is to take such steps as appear reasonable to protect the register from interference, unauthorised access, or damage.

Subsection (5) enables the Scottish Ministers, in consultation with the Keeper, to prescribe fees in relation to the RSP.

Structure

88 The parts of the Register of Statutory Pledges

The Keeper must make up and maintain, as parts of the register—

(a) the statutory pledges record, and

(b) the archive record.

NOTE

This section provides for the RSP to be kept in two parts, being the statutory pledges record and the archive record conform to sections 89 and 90 of the Bill.

See paragraph 30.2 of the Report.

89 The statutory pledges record of the Register of Statutory Pledges

(1) An entry in the statutory pledges record is to include—

(a) the provider's name and address,

(b) where the provider is an individual, the provider's date of birth,

(c) any number which the provider bears and which, by virtue of RSP Rules, must be included in the entry,

(d) the secured creditor's name and address,

(e) any number which the secured creditor bears and which, by virtue of RSP Rules, must be included in the entry,

(f) where the secured creditor is not an individual, an address (which may be an e-mail address) to which any request for information regarding the statutory pledge may be sent,

(g) such description of the encumbered property as may be—

(i) required, or

(ii) permitted,

for the purposes of this subsection by RSP Rules,

(h) a copy of the constitutive document of the statutory pledge,

(i) the registration number allocated under section 91(4)(b) to the entry for the statutory pledge,

(j) where the statutory pledge has been amended in pursuance of section 60(7), a copy of the amendment document,

(k) the date and time of registration of—

(i) the statutory pledge, and

(ii) any amendment to the statutory pledge, and

(l) such other data as may be required by virtue of any other section of this Act (including, without prejudice to the generality of this paragraph, such other information as may be specified for the purposes of this subsection by RSP Rules).

(2) The statutory pledges record is the totality of all such entries.

NOTE

This section provides for the information to be included by the Keeper in an entry for a statutory pledge in the statutory pledges record, and for the record to be comprised of the totality of such entries.

Some of that information will be as specified in, or determined under, rules made by the Scottish Ministers by regulations under section 114 of the Bill ("RSP Rules").

See paragraphs 30.4 to 30.10 of the Report.

90 The archive record of the Register of Statutory Pledges

The archive record—

(a) is the totality of all entries transferred from the statutory pledges record—

(i) under section 100(6), 101(11) or (12), 102(4) or 103(4), or

(ii) by virtue of section 99(1)(a), and

(b) includes such other data as may be specified for the purposes of this section by RSP Rules.

NOTE

This section has the effect that the archive record will comprise the totality of all entries formerly in the statutory pledges record which are archived in accordance with Chapter 2 of Part 2 of the Bill.

The archive record may also include such other data as is specified by the Scottish Ministers in RSP Rules.

See paragraphs 35.50 to 35.52 of the Report.

Applications for registration

91 Application for registration of statutory pledge

(1) An application for registration of a statutory pledge may be made to the Keeper by the secured creditor.

(2) The Keeper must accept the application if—

(a) it—

(i) conforms to such RSP Rules as may relate to the application, and

(ii) is submitted with a copy of the constitutive document,

(b) the Keeper has such data as the Keeper requires, by virtue of section 89, to make up an entry for the statutory pledge, and

(c) either—

(i) such fee as is payable for the registration is paid, or

(ii) arrangements satisfactory to the Keeper are made for payment of that fee.

(3) If the requirements of any of paragraphs (a) to (c) of subsection (2) are not satisfied, the Keeper must reject the application and inform the applicant accordingly.

(4) On accepting an application made under subsection (1), the Keeper—

(a) must—

(i) make up an entry for the statutory pledge (from the constitutive document, the data provided in the application and the circumstances of registration), and

(ii) maintain the entry in the statutory pledges record, and

(b) must allocate a registration number to the entry.

NOTE

This section provides for the secured creditor to be able to apply to the Keeper for registration of a statutory pledge in the RSP.

Subsections (2) and (3) have the effect that the Keeper must accept an application that is conform to this section, and reject an application that does not so conform. See paragraphs 29.13 and 29.14 of the Report, as regards the constitutive document.

Subsection (4) imposes a duty on the Keeper to make up an entry in the statutory pledges record for an application that is accepted, and to allocate a registration number to the entry.

See paragraphs 30.11 to 30.16 of the Report.

92 Other applications for registration

(1) A secured creditor may apply to the Keeper for registration of an amendment to a statutory pledge—

(a) to add property to the encumbered property, or

(b) to increase the extent of the secured obligation.

(2) The Keeper must accept the application if—

(a) it conforms to such RSP Rules as may relate to the application,

(b) it is submitted with a copy of the amendment document,

(c) the Keeper has such data as the Keeper requires, by virtue of section 89, to revise the entry to which the application relates, and

(d) either—

(i) such fee as is payable for the registration is paid, or

(ii) arrangements satisfactory to the Keeper are made for payment of that fee.

(3) If the requirements of any of paragraphs (a) to (d) of subsection (2) are not satisfied, the Keeper must reject the application and inform the applicant accordingly.

(4) If the application is accepted, the Keeper must revise the entry for the statutory pledge accordingly.

NOTE

This section provides for the secured creditor to be able to apply to the Keeper for registration in the RSP of an amendment of a statutory pledge, as specified in subsection (1).

Section 60(1) of the Bill has the effect that a statutory pledge may only be amended by an amendment document as defined in that section. It follows that where an amendment is registered the application to register should be submitted with a copy of the amendment document.

Separately, the pledge may be restricted or discharged off-register by way of a written statement under section 61(1) of the Bill. The RSP may be corrected for any such change by an application under section 100 of the Bill. The Keeper may also correct the RSP under section 102 if she becomes aware of a manifest inaccuracy in the RSP (and see section 116(4) of the Bill for the meaning of "inaccuracy").

Subsections (2) and (3) have the effect that the Keeper must accept an application that is conform to this section, and reject an application that does not so conform. See paragraphs 29.13 and 29.14 of the Report, as regards the amendment document.

See in general paragraphs 30.17 to 30.20 of the Report.

Verification statement and date and time of registration

93 Verification statement as to registration of statutory pledge or of amendment to statutory pledge

(1) The Keeper must, after the registration, by virtue of an application made—

(a) under section 91(1), of a statutory pledge, or

(b) under section 92(1), of an amendment to a statutory pledge,

issue to the applicant a written statement verifying the registration.

(2) That statement must—

(a) conform to such RSP Rules as may relate to the statement, and

(b) include—

(i) the date and time of the registration, and

(ii) the registration number allocated to the entry to which the application relates.

(3) Where a statement has been issued under subsection (1), the provider may request from the secured creditor a copy of that statement.

(4) Within 21 days after a request is made under subsection (3), the secured creditor must supply the provider with the copy requested.

NOTE

This section provides for the Keeper to issue a verification statement to the applicant after registering or amending a statutory pledge under sections 91 or 92 of the Bill.

The statement must be conform to any requirement prescribed in RSP Rules, and the provider may request a copy of the statement from the secured creditor.

See paragraphs 30.22 to 30.24 of the Report.

94 Date and time of registration of statutory pledge or of amendment to statutory pledge

(1) A statutory pledge is taken to be registered on the date and at the time which are entered for it by virtue of section 89(1)(k)(i).

(2) An amendment to a statutory pledge is taken to be registered on the date and at the time which are entered for it by virtue of section 89(1)(k)(ii).

(3) The Keeper must—

(a) deal with applications for the registration of statutory pledges in the order in which they are received, and

(b) allocate the unique registration numbers of the entries to which those applications relate accordingly.

NOTE

Subsections (1) and (2) have the effect that a statutory pledge, or an amendment of a pledge, is deemed to have been registered or entered on the date and time entered in the entry for the pledge in the statutory pledges record.

Subsection (3) sets out that the Keeper must deal with applications for registration in the order in which they are received, and allocate registration numbers accordingly. The effect is that pledges which rank by registration will rank in date order.

See paragraph 30.25 of the Report.

Effective registration

95 Effective registration of statutory pledge

(1) The registration of a statutory pledge is ineffective if—

(a) the entry made up for the statutory pledge in the statutory pledges record does not include a copy of the constitutive document,

(b) the data included, by virtue of section 89(1), in that entry contains an inaccuracy which, as at the time of registration, is seriously misleading, or

(c) the constitutive document is invalid.

(2) But paragraph (b) of subsection (1) is subject to section 98(7) to (9).

(3) A registration ineffective by virtue of subsection (1) becomes effective if and when the entry is corrected.

NOTE

This section provides for the registration of a statutory pledge in the RSP to be ineffective if the entry in the statutory pledges record does not include a copy of the constitutive document, if at the time of registration the entry contains an inaccuracy that is seriously misleading, or if the constitutive document is invalid (for example, because it is a forgery).

The effect of determining whether or not an entry is seriously misleading as at the time of registration is that a supervening inaccuracy will not render the entry ineffective (although see section 97 of the Bill in that respect).

The effect of a registration being ineffective is that the statutory pledge is not created by the purported registration.

Section 98(1), (2) and (6) of the Bill provides for the meaning of the term "seriously misleading".

Subsection (2) makes subsection (1) subject to section 98(7) to (9), with the effect that a registration may be partially effective as regards the encumbered property or co-providers or co-creditors.

Subsection (3) has the effect that if a registration that is ineffective at the time of registration can be made effective by correction under this Chapter, then at that point the pledge is created.

See paragraphs 31.2 to 31.4, and 33.35 to 33.37, of the Report.

96 Effective registration of amendment to statutory pledge

(1) The registration of an amendment to a statutory pledge is ineffective if—

(a) the entry, in the statutory pledges record, for the statutory pledge does not include a copy of the amendment document,

(b) the data included, by virtue of section 89(1), in that entry contains, in consequence of the amendment, an inaccuracy which is seriously misleading, or

(c) the amendment document is invalid.

(2) But paragraph (b) of subsection (1) is subject to section 98(7) to (9).

(3) A registration ineffective by virtue of subsection (1) becomes effective if and when the entry as amended is corrected.

NOTE

This section makes the same provision for the registration of an amendment of a statutory pledge as section 95 of the Bill does for registration of the pledge.

See paragraphs 31.5 and 31.6, and 33.35 to 33.37, of the Report.

97 Supervening inaccuracies: protection of third parties

(1) Subsection (2) applies where—

(a) a statutory pledge is registered effectively over property (not being property bearing a number which must or may, by virtue of section 114(1)(c)(ii), be used in identifying it),

(b) at some time after the statutory pledge is so registered, the statutory pledges record comes to contain an inaccuracy—

(i) in the entry for the statutory pledge, being an inaccuracy which is seriously misleading (whether or not in respect of all the encumbered property), or

(ii) by virtue of the removal of the entry for the statutory pledge (whether or not on transfer of that entry to the archive record), and

(c) during the period in which the record contains that inaccuracy, a person acquires, for value, in good faith and exercising reasonable care—

(i) some or all, or

(ii) a right in some or all,

of the encumbered property in respect of which the inaccuracy is seriously misleading.

(2) On the acquisition the statutory pledge is extinguished as regards the property—

(a) acquired, or

(b) in which the right is acquired.

NOTE

This section protects a person who in good faith acquires encumbered property, or a right in encumbered property, in circumstances where the entry in the statutory pledges record comes to include after registration:

(a) an inaccuracy that is seriously misleading, or

(b) an inaccuracy by reason of the removal of an entry from the record.

This could be the case where, for example, the provider marries after the pledge is registered and changes his or her name.

The effect of this section is that the pledge will be extinguished as regards so much of the encumbered property as is property in respect of which the inaccuracy is seriously misleading upon the property being transferred.

Example — In year 1 Rachel Smith grants a statutory pledge to Mark over any piano she might acquire. Mark registers the pledge, and in year 2 Rachel acquires a piano which becomes encumbered property. She also marries, and changes her name to Rachel Jones. In year 3 Rachel sells the piano to Luke, who is in good faith, and does not know that Rachel Jones was once known as Rachel Smith. A search against Rachel Jones will not reveal the pledge, and so he will acquire the piano unencumbered by the pledge.

This protection does not apply where the encumbered property is property that is required by RSP Rules to be identified by an unique number, such as a vehicle identity number (VIN). Any person intending to acquire such an asset could readily obtain information about the pledge by searching the statutory pledges record against the VIN.

See paragraph 32.51, and Chapter 32 generally, of the Report.

98 Seriously misleading inaccuracies in entries in the statutory pledges record

(1) For the purposes of section 95(1)(b), 96(1)(b) or 97(1), an inaccuracy in an entry in the statutory pledges record is seriously misleading—

(a) if a search of that record in accordance with—

(i) section 106(2)(a)(i) for the provider's proper name, or

(ii) section 106(2)(a)(ii) for the provider's proper name and the provider's date of birth,

using the search facility provided under section 107(1)(a) does not disclose the entry, or

(b) where the provider is a person required by RSP Rules to be identified in that record by a unique number, if a search of that record for that number—

(i) in accordance with section 106(2)(a)(iii), and

(ii) using the search facility provided under section 107(1)(a),

does not disclose the entry, or

(c) in respect of so much of the encumbered property as bears a unique number which must, by virtue of RSP Rules, be included in the statutory pledges record if a search of that record for that number—

(i) in accordance with section 106(2)(a)(iv), and

(ii) using the search facility provided under section 107(1)(a),

does not disclose the entry.

(2) Subsection (1)—

(a) is subject to subsection (3), and

(b) is without prejudice to the generality of sections 95(1)(b), 96(1)(b) and 97(1).

(3) Where a search such as is mentioned in paragraph (b) of subsection (1)—

(a) discloses an entry, it is immaterial that a search such as is mentioned in paragraph (a) of that subsection does not disclose the entry,

(b) does not disclose an entry, it is immaterial that a search such as is mentioned in paragraph (a) of that subsection discloses the entry.

(4) Subject to subsection (8), subsections (1) to (3) apply in relation to a search for—

(a) a co-provider's proper name,

(b) a co-provider's—

(i) proper name, and

(ii) date of birth, or

(c) a unique number by which a co-provider is identified,

as they apply in relation to the searches mentioned in subsection (1)(a) or (b).

(5) Without prejudice to section 95(1)(a), in determining whether an inaccuracy in an entry in the statutory pledges record is seriously misleading no account is to be taken of the constitutive document, or of any amendment document, included in the entry.

(6) An inaccuracy in an entry in the statutory pledges record may be seriously misleading irrespective of whether any person has been misled.

(7) Where an inaccuracy in an entry in the statutory pledges record is seriously misleading in respect of only part of the encumbered property, that inaccuracy does not affect the entry in its application to the rest of the property.

(8) Where—

(a) the provider consists of two or more co-providers, and

(b) there is an inaccuracy in an entry in the statutory pledges record, being an inaccuracy which is seriously misleading in respect of a co-provider but not in respect of both (or all) the co-providers,

that inaccuracy does not affect the entry in its application to a co-provider in respect of whom the inaccuracy is not seriously misleading.

(9) Subsection (8) applies in relation to a secured creditor which consists of two or more co-secured creditors as it applies in relation to a provider which consists of two or more co-providers.

(10) The Scottish Ministers may by regulations amend this section by specifying further instances in which, for the purposes of section 95(1)(b), 96(1)(b) or 97(1)(b), an inaccuracy in an entry is seriously misleading.

(11) References—

(a) in subsection (1)(a) to "the provider's proper name", or

(b) in subsection (4)(a) or (b) to "a co-provider's proper name",

are to the person's name in the form determined in accordance with rules under section 114(1)(c)(i).

NOTE

This section makes further provision for the meaning of "seriously misleading" inaccuracy for the purposes of sections 95 to 97 of the Bill. The "seriously misleading" test is a feature of analogous schemes for security over moveables, such as UCC–9.

If a registration contains an inaccuracy that prevents it being disclosed by a properly formatted search, the inaccuracy should generally be regarded as being seriously misleading. This section sets out some of the circumstances in which an entry will be seriously misleading, but leaves open the possibility that the statutory pledges record will contain other types of seriously misleading inaccuracy.

For example, there may be an inaccuracy in the name or address of a secured creditor such that an entitled person is unable to make an information request under section 110 of the Bill. Such an inaccuracy is likely to be seriously misleading, with the effect that the entry is ineffective and the pledge is not created by registration.

Subsections (1) and (2) have the effect that an entry in the statutory pledges record is seriously misleading if a search using any of the criteria specified in this subsection fails to disclose the entry. The criteria are:

(a) The proper name of the provider,

(b) The unique number of any provider that is required by RSP Rules to be identified by such a number (which might include for example the registration number of a limited company), or

(c) The unique number for encumbered property that is required by RSP Rules to be identified by such a number (which might include for example a vehicle identification number or the registration number for a patent or trademark).

The search must be in accordance with searches of the RSP as permitted under section 106 of the Bill, which the Keeper is required by section 107 of the Bill to make available to any person requiring such a search.

Subsection (5) has the effect that in determining whether an entry is seriously misleading no account is to be taken of the constitutive document or any amendment document. This is needed because a search under sections 106 and 107 will not extend to the content of those documents.

Subsection (6) provides that the test for whether an inaccuracy is seriously misleading is an objective test, in that no account is to be taken of whether any persons has in fact been misled by an entry.

Subsections (7) to (9) provide for entries that are misleading only in some respects, and have the effect that a registration may be partly effective.

Subsection (10) enables the Scottish Minsters by regulations to specify further instances in which an entry will have a seriously misleading inaccuracy for the purposes of this section.

Subsection (9) has the effect that the proper name of a person for the purpose of this section will be determined in accordance with RSP Rules.

See paragraphs 31.7 to 31.18 of the Report.

Duration

99 Power of Scottish Ministers as regards duration of statutory pledge

(1) The Scottish Ministers may by regulations—

(a) specify a period from the creation (or renewal by virtue of paragraph (b)) of an entry in the statutory pledges record, being a period at the end of which, unless the entry has during that period been—

(i) renewed (or as the case may be further renewed) by virtue of that paragraph, or

(ii) removed,

the statutory pledge to which the entry relates will be extinguished and the entry removed, and

(b) enable application to be made by the secured creditor for the renewal of an entry which would otherwise fall to be removed by virtue of paragraph (a).

(2) Different provision may be made by virtue of subsection (1) for different cases or for different classes of case.

(3) Before exercising powers under this section, the Scottish Ministers must consult the Keeper.

NOTE

This section provides for the Scottish Ministers, in consultation with the Keeper of the Registers of Scotland, to be able by regulations to specify a period at the end of which an entry in the statutory pledges record will be deleted and the statutory pledge extinguished.

This power could be used, for example, in the event that a large number of pledges believed to have been extinguished or restricted off-register continue to appear in the record many years after registration. Similar powers are seen in comparator legislation in other jurisdictions.

See paragraphs 35.20 to 35.29 of the Report.

100 Application to Keeper by secured creditor for correction of statutory pledges record

(1) An application may be made to the Keeper for the correction of an entry in the statutory pledges record, being an entry as regards which the applicant is the secured creditor (whether or not identified as such in the entry).

(2) The Keeper must accept an application under subsection (1) provided that—

(a) the application conforms to what is prescribed, for the purposes of this section, in RSP Rules, and

(b) either—

(i) such fee as is payable for the correction in question is paid, or

(ii) arrangements satisfactory to the Keeper are made for payment of that fee.

(3) If the requirements of either of paragraphs (a) and (b) of subsection (2) are not satisfied, the Keeper must reject the application and inform the applicant accordingly.

(4) On accepting, by virtue of subsection (2), an application for the correction of the statutory pledges record, the Keeper must—

(a) correct the entry accordingly, and

(b) issue to the applicant and to the provider a written statement verifying the correction.

(5) That statement must—

(a) conform to such RSP Rules as may relate to the statement, and

(b) include—

(i) the date and time of the correction, and

(ii) the registration number allocated to the entry.

(6) Where, under subsection (4), the Keeper corrects the record by—

(a) removing the entry, the Keeper must transfer the entry to the archive record and note on the transferred entry—

(i) that the transfer is in consequence of a correction under that subsection, and

(ii) the date and time of the removal, or

(b) removing or replacing data included in the entry or by replacing a copy document, the Keeper must note on the entry—

(i) that it has been corrected, and

(ii) the details of the correction (including, without prejudice to the generality of this paragraph, the date and time of the correction),

and in the case of the removal of the copy document, must transfer the copy to the archive record and retain it there.

(7) Without prejudice to the generality of subsection (1), in that subsection "secured creditor" includes, if the statutory pledge has been assigned, the person who was the secured creditor before the assignation.

NOTE

Subsection (1) enables the secured creditor, and only the creditor, to apply to the Keeper for correction of an entry for a statutory pledge in the statutory pledges record.

The secured creditor does not for that purpose need to be identified as such in the entry in the statutory pledges record. There are a number of reasons why the creditor might not be so identified, including an error at the time of registration, a change of name, or an assignation of the pledge (see section 59 of the Bill).

So for example an assignee as a successor in title to the right of the secured creditor (see section 116(1) of the Bill) may apply for correction. Alternatively, subsection (7) has the effect that the assignor of a pledge can also apply for a correction.

The Keeper must accept an application that conforms to subsection (2), and reject one that does not.

Subsections (4) and (5) provide that the Keeper must on accepting an application correct the entry (and note in the entry that this has been done), and issue to the applicant a verification statement in the form required by RSP Rules.

Subsection (6) provides for the Keeper to correct the record as required to give effect to an application for correction that is accepted by the Keeper.

See paragraphs 33.11 to 33.22 of the Report.

101 Demand that application be made for a correction to the statutory pledges record by the removal of an entry or of data included in an entry

(1) A person (in this section referred to as "D")—

(a) identified as the provider, or as a co-provider, of a statutory pledge in an entry in the statutory pledges record, or

(b) with a right in property identified as the encumbered property in an entry in the statutory pledges record,

and who considers that the circumstances are as mentioned in subsection (2), may issue a demand in a prescribed form to the person identified in that entry as the secured creditor (the person so identified being in this section referred to as "ISC"), that ISC apply to the Keeper for the correction of the statutory pledges record.

(2) Those circumstances are, that—

(a) D is neither the provider, nor a co-provider, of the statutory pledge, or

(b) all or part of the property identified in the entry as the encumbered property is not encumbered property.

(3) A demand issued under subsection (1) is to specify a period (being a period of not less than 21 days after it is received) within which it is to be complied with.

(4) ISC may not charge a fee for such compliance.

(5) If ISC fails to comply with the demand within the period specified by virtue of subsection (3), D may apply to the Keeper for the correction of the statutory pledges record.

(6) Any application under subsection (5) must conform to such RSP Rules as may relate to the application.

(7) On receiving an application under subsection (5) the Keeper must—

(a) serve a notice on ISC stating that the Keeper intends to correct the record on a date specified in the notice (being a date no fewer than 21 days after the date of the notice),

(b) note on the entry that the application has been received and include in that note—

(i) the details of the correction sought, and

(ii) the date on which the application was received,

(c) issue to D a written statement verifying that the application has been received, and

(d) notify the person identified in the entry as the provider (if a different person from D) that the notice mentioned in paragraph (a) has been served on ISC.

(8) ISC—

(a) may, before the date specified under subsection (7)(a), apply opposing the making of the correction to the court, and

(b) on making any such application must notify the Keeper accordingly.

(9) Subject to subsection (10), the court, on an application under (8)(a), may if satisfied that the correction—

(a) is not justified, direct that no change be made to the record in consequence of the application under subsection (5), or

(b) is justified in whole or in part, direct that the record be corrected accordingly.

(10) The court is not to make a direction under subsection (9) unless satisfied that before the date specified under subsection (7)(a) the Keeper received notification, under subsection (8)(b), of the application.

(11) If the Keeper does not receive before the date specified under subsection (7)(a) notification, under subsection (8)(b), of an application under subsection (8)(a) opposing the making of the correction, the Keeper is on that date to make the correction.

(12) Where, by virtue of subsection (9)(b) or under subsection (11), the Keeper corrects the record by—

(a) removing the entry from the statutory pledges record, the Keeper must transfer the entry to the archive record and note on the transferred entry—

(i) that the transfer is in consequence of a correction by virtue of (or as the case may be, under) the subsection in question, and

(ii) the date and time of the removal of the entry from the , or

(b) removing data included in the entry or removing a copy document, the Keeper must note on the entry—

(i) that it has been corrected, and

(ii) the details of the correction (including, without prejudice to the generality of this paragraph, the date and time of the correction),

and in the case of the removal of the copy document, must transfer the copy to the archive record and retain it there.

(13) Where, by virtue of subsection (9)(b) or under subsection (11), the Keeper effects a correction, the Keeper must notify (in so far as it is reasonable and practicable to do so)—

(a) every person specified for the purposes of this subsection by RSP Rules, and

(b) any other person whom the Keeper considers it appropriate to notify,

that the correction has been effected.

NOTE

This section enables a person with a specified interest in the accuracy of the statutory pledges record, and who maintains that the record is inaccurate, to be able to:

(a) demand that the secured creditor apply to the Keeper within at least 21 days for a correction of the record under section 100 of the Bill, and

(b) if no application is made, for that person to be able to apply for the correction.

Subsections (1) and (2) have the effect that a person identified in the record as the provider or a co-provider, or a person with a right in property identified as the encumbered property, can make a demand on the secured creditor if they assert that they are not a provider or the property is not encumbered property.

Example 1 An entry states that a statutory pledge has been created over the car with VIN 12345. In fact, the statutory pledge was created over the car with VIN 12335. The owner of the car with VIN 12345 can demand a correction.

Example 2 An entry states that a statutory pledge has been created over a car with VIN 12335. This was accurate as at the date of registration, but the secured creditor has subsequently been discharged off-register. The provider can demand correction.

In the event an application is made following a failure to comply then the Keeper must serve a notice on the secured creditor intimating that the record will be corrected on a specified date. The secured creditor may apply to the court before that date opposing the making of the correction (for which see subsections (8) to (11)).

The Keeper cannot make any correction until the application to the court has been determined. The Keeper can if desired enter the court process (see section 104 of the Bill).

Subsections (12) and (13) provide for notification of any correction, and for giving effect to the correction as appropriate in the statutory pledges record or archive record.

The person identified as the secured creditor in the entry in the statutory pledges record may no longer be the creditor because the pledge has been assigned. This section does not impose an express duty on any such person either to inform the person making the demand that they are not the true creditor, or to inform the true creditor (if known) that a demand has been made. However, a failure to do so may under the general law cause the apparent creditor to be liable for any loss sustained as a result of the Keeper making a correction that was not required.

See paragraphs 33.23 to 33.34 of the Report.

102 Correction of statutory pledges record where Keeper becomes aware of manifest inaccuracy

(1) This section applies where the Keeper becomes aware of a manifest inaccuracy in the statutory pledges record.

(2) The Keeper must correct the record if what is needed to correct it is manifest.

(3) Where what is needed to correct it is not manifest, the Keeper must note the inaccuracy on the entry in question.

(4) Where under subsection (2) the Keeper corrects the record by—

(a) removing the entry from the statutory pledges record, the Keeper must transfer the entry to the archive record and note on the transferred entry—

(i) that the transfer is in consequence of a correction under that subsection, and

(ii) the date and time of the removal, or

(b) removing or replacing data included in the entry or by replacing a copy document, the Keeper must note on the entry—

(i) that it has been corrected, and

(ii) the details of the correction (including, without prejudice to the generality of this paragraph, the date and time of the correction),

and in the case of the replacement of the copy document, must transfer the replaced copy to the archive record and retain it there.

(5) Where under subsection (2) the Keeper effects a correction, the Keeper must notify (in so far as it is reasonable and practicable to do so)—

(a) every person specified for the purposes of this subsection by RSP Rules, and

(b) any other person whom the Keeper considers it appropriate to notify,

that the correction has been effected.

NOTE

Subsections (1) and (2) of this section provide for the Keeper to correct a manifest inaccuracy in the statutory pledges record, where what is needed to correct the inaccuracy is also manifest.

Subsection (3) provides for the Keeper to note any inaccuracy that cannot be corrected.

Subsections (4) and (5) provide for notification of any correction, and for giving effect to the correction as appropriate in the statutory pledges record or archive record.

See paragraphs 33.6 and 33.7 of the Report.

103 Directions for, or in relation to, correction of the statutory pledges record

(1) This section applies where, in any proceedings, a court determines that the statutory pledges record is inaccurate.

(2) The court must direct the Keeper to correct the record.

(3) In connection with any such correction, the court may give the Keeper such further direction (if any) as it considers requisite.

(4) Where by virtue of subsection (2) the Keeper effects a correction by—

(a) removing the entry in question from the statutory pledges record, the Keeper must transfer the entry to the archive record and note on the transferred entry—

(i) that the transfer is in pursuance of the direction of a court under subsection (2), and

(ii) the date and time of the removal of the entry from the statutory pledges record, or

(b) removing or replacing data included in the entry or by replacing a copy document, the Keeper must note on the relevant entry—

(i) that it has been corrected, and

(ii) the details of the correction (including, without prejudice to the generality of this paragraph, the date and time of the correction),

and in the case of the replacement of the copy document, must transfer the replaced copy to the archive record and retain it there.

(5) Where by virtue of subsection (2) the Keeper effects a correction, the Keeper must notify (in so far as it is reasonable and practicable to do so)—

(a) every person specified for the purposes of this subsection by RSP Rules, and

(b) any other person whom the Keeper considers it appropriate to notify,

that the correction has been effected.

NOTE

This section ensures both that the courts can where appropriate direct the Keeper to correct an entry in the RSP, and that the Keeper must comply with such a direction.

The Bill does not provide for an express right of appeal against or review of any decision by the Keeper. An issue relating to the accuracy of the register might however be raised in other proceedings, such as a judicial review of a decision by the Keeper, or proceedings in which it is alleged that a constitutive document is a forgery.

Example 1 A constitutive document is reduced by the court because it has been forged by one of the apparent parties. The court can direct the Keeper to correct the entry in the statutory pledges record.

Example 2 An entry has been created in the statutory pledges record for a security by Andrew in favour of Bruce. But in the application form for registration of the assignation Bruce erroneously states that Carol is the creditor. Carol could seek removal of the entry by the court (as an alternative to a demand for a correction).

See paragraphs 33.8 and 33.9 of the Report.

104 Proceedings involving the accuracy of the statutory pledges record

The Keeper is entitled to appear and be heard in any civil proceedings, whether before a court or before a tribunal, in which is put in question (either or both)—

(a) the accuracy of the statutory pledges record,

(b) what is needed to correct an inaccuracy in that record.

NOTE

See paragraph 33.10 of the Report.

105 Correction of statutory pledges record: general

(1) In this Part, any reference to "correction" includes (without prejudice to the generality of that expression and except in so far as the context otherwise requires)—

(a) the removal of data included in an entry,

(b) the removal of an entry from the statutory pledges record and the transfer of that entry to the archive record,

(c) the replacement of data, or of a copy document, included in an entry,

(d) the restoration of data, or of a copy document, to an entry, and

(e) the restoration of an entry (whether or not by removing it from the archive record and transferring it to the statutory pledges record);

and analogous expressions are to be construed accordingly.

(2) A correction is taken to be made on the date and at the time which are entered for it in the register in pursuance of a provision of this Part of this Act.

NOTE

This section deals with some general matters in relation to corrections.

Subsection (1) sets out a non-exhaustive list of the various types of correction that are competent, although not all these types are relevant to all of the preceding provisions. See paragraphs 33.4 and 33.5 of the Report.

Subsection (2) sets out what is taken to be the date and time of correction. This is particularly important as regards sections 95 and 96 of the Bill, under which an ineffective registration may be made effective by correction (so creating the pledge). See paragraph 33.38 of the Report.

Searches and extracts

106 Searching the statutory pledges record

(1) Any person may search the statutory pledges record provided that—

(a) the search accords with—

(i) subsection (2), and

(ii) such RSP Rules as are made under section 114(1)(h), and

(b) either—

(i) such fee as is payable for the search is paid, or

(ii) arrangements satisfactory to the Keeper are made for payment of that fee.

(2) The statutory pledges record may be searched only—

(a) by reference to any of the following data in the entries contained in that record—

(i) the names of providers,

(ii) the names and dates of birth of providers who are individuals,

(iii) the unique numbers of providers required by RSP Rules to be identified in the statutory pledges record by such a number,

(iv) if RSP Rules require or permit the encumbered property to be identified (whether by a number unique to that property or in some other way), by reference to such identification,

(b) by reference to registration numbers allocated, under section 91(4)(b), to entries in that record, or

(c) by reference to some other factor, or characteristic, specified for the purposes of this paragraph by RSP Rules.

NOTE

This section provides that any person may search the statutory pledges record on payment of any search fee, provided that the search accords with RSP Rules, and that it is one of the types of search permitted under subsection (2).

Subsection (2)(a) sets out that a search can be made by reference to the name of the provider, or (in the case of an individual) their name and date of birth, unique number for the provider (where RSP Rules require identification by number) or unique number of the encumbered property (where RSP Rules require or permit identification by number).

Subsection (2)(b) and (c) set out that a search may be against the registration number of the pledge and any other factor or characteristic specified in RSP Rules.

It will not be possible to search against the secured creditor, or to search in the archive record, unless the Scottish Ministers made provision in RSP Rules permitting such searches. It will, however, be possible to obtain an extract of an entry in the archive record under section 109 of the Bill.

It will also not be possible to search against date of birth alone, in order to reduce the risk of fraud through identity theft. The Scottish Ministers will also be able through RSP Rules to prevent dates of birth from being disclosed on the face of the Register, or to limit the number of searches by reference to the same name and different dates of birth that can be made in a particular time period.

See paragraphs 34.2 to 34.9 of the Report.

107 Keeper's duties and powers as regards the provision of facilities for searching the statutory pledges record

(1) The Keeper—

(a) must for the purposes of section 106 provide a search facility the search criteria of which are specified by RSP Rules, and

(b) may provide such other search facilities, with such other search criteria, as the Keeper thinks fit.

(2) In subsection (1), "search criteria" means the criteria in accordance with which what is searched for must match data in an entry in order to retrieve that entry.

NOTE

This section sets out that the Keeper must provide a search facility using criteria specified in RSP Rules, and may provide a search facility using other criteria.

The Keeper has in that latter respect the power under section 108 of the Land Registration etc. (Scotland) Act 2012 to provide commercial services, on such terms as may be agreed between the Keeper and those to whom the services are provided.

Sections 95 to 97 of the Bill have the effect that it must be possible to carry out searches for the purposes of the "seriously misleading" test, as provided for under those sections. It will therefore be for Ministers to make such RSP Rules as are needed under this section for those purposes.

Subsection (2) sets out that "search criteria" means the criteria in accordance with which what is searched for must match data in an entry in order to retrieve the entry.

RSP Rules will, amongst other matters, be able to determine whether the search criteria will provide for an exact match or a close match search.

Example — A search against "John A Smith" would return a match against John Smith if RSP Rules set out that the search criteria do not require a match with middle initials. However, it would not return a match against John A Smythe if the criteria require an exact match for the last name.

See paragraphs 34.10 and 34.11 of the Report.

108 Statutory pledges record: printed search results and their evidential status

A printed search result which relates to a search carried out by means of a search facility provided by the Keeper and which purports to show an entry in the statutory pledges record is admissible in evidence and, in the absence of evidence to the contrary, is sufficient proof of (as the case may be)—

(a) the registration of—

(i) the statutory pledge, or

(ii) an amendment to the entry in the statutory pledges record,

to which the result relates,

(b) a correction of the entry in the statutory pledges record to which the result relates, and

(c) the date and time of such registration or correction.

NOTE

This section enables printed search results obtained from the Keeper to be used as evidence of certain matters and, moreover, to have the effect of proving certain matters unless there is evidence to the contrary. There are similar provisions for other jurisdictions in their PPSA schemes.

This section should be read with section 109, which provides for an extract from the Registers, and which would provide conclusive evidence of the contents of the relevant entry at the date the extract is issued.

See paragraphs 34.12 and 34.13 of the Report.

109 Register of Statutory Pledges: extracts and their evidential status

(1) Any person may apply to the Keeper for an extract of an entry in the register.

(2) The Keeper must issue the extract if—

(a) such fee as is payable for issuing it is paid, or

(b) arrangements satisfactory to the Keeper are made for payment of that fee.

(3) The Keeper may validate the extract as the Keeper considers appropriate.

(4) The Keeper may issue the extract as an electronic document if the applicant does not request that it be issued as a traditional document.

(5) The extract is to be accepted for all purposes as sufficient evidence of the contents of the entry as at the date on which and the time at which the extract is issued (being a date and time specified in the extract).

NOTE

This section provides for it to be possible to obtain an extract from the Keeper of any entry or part of an entry in the RSP, on payment of any fee (or making an arrangement to pay).

An extract is sufficient evidence of the contents of an entry at the time the extract is issued, and can be used for that purpose in for example any court proceedings.

See paragraphs 34.14 and 34.15 of the Report.

Request for information

110 Secured creditor's duty to respond to request for information

(1) An entitled person may request the person identified in the entry for a statutory pledge as the secured creditor (the person so identified being in this section referred to as "ISC") to provide the entitled person—

(a) if ISC is the secured creditor, with a written statement (either or both)—

(i) as to whether or not property specified by the entitled person is, or is part of, the encumbered property,

(ii) describing the secured obligation, or

(b) if ISC—

(i) is no longer the secured creditor, with information to that effect, with the name and address of the person to whom ISC assigned the statutory pledge and (as the case may be and in so far as known) with the names and addresses of subsequent assignees, or

(ii) has never been the secured creditor, with information to that effect.

(2) The following are "entitled persons" for the purposes of this section—

(a) a person who has a right in the property so specified,

(b) a person who has a right to execute diligence against the property so specified (or who is authorised by decree to execute a charge for payment and will have the right to execute diligence against that property if and when the days of charge expire without payment), and

(c) a person who is not mentioned in paragraph (a) or (b) but—

(i) is prescribed under this paragraph, or

(ii) has the consent of the person identified in the entry as the provider to make a request under paragraph (a) or (b) of subsection (1).

(3) Subject to subsection (5), ISC must, within 21 days after receiving a request by virtue of subsection (1), comply with that request unless subsection (7) applies.

(4) ISC may recover from the entitled person any costs reasonably incurred in complying with the request.

(5) The court, if satisfied that in all the circumstances it would be unreasonable to require ISC—

(a) to comply with the request (whether in whole or in part), may by order, on the application of ISC, exempt ISC from complying with—

(i) the request, or

(ii) such part of the request as it may specify in the order, or

(b) to comply with the request within the 21 days mentioned in subsection (3), may by order, on such application, extend by such number of days as it may specify in the order the period within which ISC must comply with the request.

(6) If the court is satisfied on the application of the entitled person that ISC, without reasonable excuse, failed to comply with subsection (3), it may by order require ISC to comply with the request within 14 days.

(7) This subsection applies—

(a) where it is manifest that the registration is ineffective as regards the statutory pledge to which the request relates,

(b) where it is manifest from the entry for the statutory pledge that the property (or any part of the property) specified under subsection (1) by the entitled person is not encumbered by that pledge,

(c) in so far as the request is for a written statement describing the secured obligation, if the extent of that obligation is manifest from the entry for the statutory pledge, or

(d) where—

(i) ISC has, within the 3 months immediately preceding ISC's receipt of the request, already complied with a request under subsection (1), by the same person and in relation to the same property, and

(ii) the information contained in the statement issued in relation to the earlier request is still correct.

(8) Subsection (9) applies where an entitled person—

(a) makes a request under subsection (1),

(b) is informed by the secured creditor, in a response under paragraph (a) of that subsection to the request, that the property specified under that subsection by the entitled person is neither the encumbered property nor part of that property, and

(c) within 3 months after being so informed acquires in good faith—

(i) the property so specified (or any part of it), or

(ii) a right in that property (or part).

(9) On that acquisition, the statutory pledge is extinguished as regards the property (or part).

(10) This section applies in relation to any secured creditor whose name and address have, by virtue of subsection (1)(b), been provided to an entitled person by ISC as it applies to ISC.

NOTE

This section enables a person with an interest in the encumbered property (the "entitled person" under subsection (2)) to be able to request from the person identified in the statutory pledges record as the secured creditor a written statement:

(a) as to whether property specified in the request is encumbered property, or

(b) describing the secured obligation.

The creditor so identified must - unless exempt under subsection (7) - provide the information within 21 days if they are still the creditor, and if not still the creditor (or they never have been) advise the entitled person accordingly. The creditor may recover their reasonable costs in that respect.

Example Adam grants a statutory pledge over his Rolls Royce. A search in the RSP against Adam reveals only the entry for that pledge. A request to the person named as secured creditor as to whether the pledge covers Adam's yacht is exempt, as it will be clear from the register that it does not.

Subsection (2) provides for the meaning of "entitled person", with the effect that it covers any person who has a right to the property specified in the request, a right to exercise diligence against that property, the consent of the provider, or is as specified in regulations made by the Scottish Ministers.

Subsection (10) makes it clear that an assignee of the secured creditor may be treated as being the creditor for the purposes of a further request under this section.

The person identified as the secured creditor may ask the court to exempt them from complying with the request, or to allow further time for doing so. The entitled person may if necessary seek an order requiring that person to comply with the request, and a continuing failure to comply would then be a contempt of court.

A duty of this type is also to be found in other schemes for security over moveables, such as the DCFR Book IX. The duty to provide information works to protect third parties who may otherwise lack sufficient information about the scope of a statutory pledge. For example, the encumbered property might be described only by reference to a class, or be intended to include assets to be acquired by the provider, so that in either case it is not clear whether or not any specific asset is encumbered.

Subsections (8) and (9) set out a special rule to protect purchasers of encumbered property, and are also influenced by the DCFR IX.–3:322(1). If a person making a request is advised wrongly by the secured creditor that the particular property is not subject to the pledge, and the person then acquires the property (or a right in it such as a further pledge) in good faith within three months, then the pledge is extinguished.

See paragraphs 35.2 to 35.19 of the Report.

Entitlement to compensation

111 Register of Statutory Pledges: liability of Keeper

(1) A person is entitled to be compensated by the Keeper for loss suffered in consequence of—

(a) an inaccuracy attributable to the Keeper—

(i) in the making up, maintenance or operation of the register, or

(ii) in an attempted correction of the register,

(b) the issue, under section 93(1) or 100(4)(b), of a written statement which is incorrect,

(c) the service, under section 101(13) or 103(6) of a notification which is incorrect, or

(d) the issue, under section 109, of an extract which is not a true extract.

(2) But the Keeper has no liability under subsection (1)—

(a) in so far as the person's loss could have been avoided had the person taken measures which it would have been reasonable for the person to take,

(b) in so far as the person's loss is not reasonably foreseeable, or

(c) for non-patrimonial loss.

NOTE

This section provides for the Keeper to compensate any person who has suffered a loss for a reason specified in subsection (1).

The liability under subsection (1) is strict in that the person does not have to show that the Keeper is at fault, but subsection (2) limits the losses that can be recovered by excluding certain types of claim.

The limitation is similar to that in section 37 of the Bill, and in section 106 of the Land Registration etc. (Scotland) Act 2012.

See paragraphs 35.33 and 35.34 of the Report.

112 Register of Statutory Pledges: liability of certain other persons

(1) Where a person (in this section referred to as "P") suffers loss in consequence of—

(a) an inaccuracy in an entry in the register (not being an inaccuracy attributable to the Keeper), P is entitled to be compensated for that loss by the person who made the application which gave rise to the entry if, in making it, that person failed to take reasonable care,

(b) an inaccuracy in information supplied in response to a request under section 110(1), P is entitled to be compensated for that loss by the person who supplied the information if, in supplying it, that person failed to take reasonable care, or

(c) a failure, without reasonable cause, to comply with a request under section 110(3), P is entitled to be compensated for that loss by the person whose failure it was.

(2) But a person has no liability under subsection (1)—

(a) in so far as P's loss could have been avoided had P taken measures which it would have been reasonable for P to take,

(b) in so far as P's loss is not reasonably foreseeable, or

(c) for non-patrimonial loss.

NOTE

This section provides for certain persons to be liable, on fault shown, for losses suffered by another person in the circumstances specified in subsection (1).

Subsection (1)(a) applies where a person suffers loss as a result of an inaccuracy in an entry where the person who made the application which led to the entry did not exercise reasonable care.

Example — Alan maliciously registers a forged constitutive document bearing to be granted by Bruce over property owned by Claire. Claire has a claim against Alan for any loss.

Subsection (1)(b) applies where as a result of a failure to take reasonable care there is an inaccuracy in responding to an information request under section 110 of the Bill.

It should be read with section 110(8) and (9) of the Bill, which provides for certain pledges to be extinguished where property is acquired within 3 months after faulty information is given to an entitled person.

Example — Information is supplied to Ailsa by Brendan that certain property is not pledged. Brendan does not take reasonable care, and the information is wrong. Ailsa takes a pledge over the property in reliance on that information. She expects that the pledge will be a first ranked security, but it is in fact subject to the existing pledge. Ailsa will have a claim against Brendan.

Subsection (1)(c) applies where a person has failed to provide information under section 110 of the Bill without reasonable cause.

Subsection (2) imposes the same restrictions on liability as those set out in section 111(2) of the Bill.

See paragraphs 35.35 and 35.36 of the Report.

Service of documents for purposes of certain provisions of this Chapter of Part 2

113 Service of documents for purposes of certain provisions of this Chapter of Part 2

In the application of section 26 of the Interpretation and Legislative Reform (Scotland) Act 2010 (service of documents) for the purposes of section 101(1), (7)(a) or (c) or (13), 103(6) or 110(1)—

(a) subsection (4) of that section of that Act is to be construed as if, for paragraphs (a) to (c) of the subsection, there were substituted the words "the address given for the person in the entry in question", and

(b) where an e-mail address for the person identified as the secured creditor is contained in the entry in question, the request or notice is to be taken to be served as mentioned in subsection (2)(c) of that section of that Act on being transmitted to that e-mail address.

NOTE

Section 26 of the Interpretation and Legislative Reform (Scotland) Act 2010 provides for the service (including sending) of documents in Acts of the Scottish Parliament.

This section modifies that section for the purposes of certain provisions in this chapter of the Bill.

Paragraph (a) refers to subsection (4) of section 26, which deals with the sending of notices. The effect of paragraph (a) is that a notice should be sent to the address for the person that is given in the register entry.

Paragraph (b) refers to subsection (2)(c) of section 26, which deals with electronic communication of notices. The effect of paragraph (b) is that where an e-mail address is given for a person in the register entry, the electronic communication should be to that e-mail address.

RSP Rules

114 RSP Rules

(1) The Scottish Ministers may by regulations make rules (in this Act referred to as "RSP Rules")—

(a) as to the making up and keeping of the register,

(b) as to procedure in relation to applications—

(i) for registration, or

(ii) for corrections,

(c) as to the identification, in any such application and in the register, of any person or of property, including—

(i) how the proper form of a person's name is to be determined, and

(ii) where the person or property bears a number (whether of numerals or of letters and numerals) unique to the person or property, whether that number must (or may) be used in identifying the person or property,

(d) as to the degree of precision with which time is to be recorded in the register,

(e) as to the manner in which an inaccuracy in the statutory pledges record may be brought to the attention of the Keeper,

(f) as to information which, though contained in a constitutive document or amendment document, need not be included in a copy of that document submitted with an application under section 91 or 92,

(g) as to whether a signature contained in a constitutive document or amendment document need be included in a copy of that document so submitted,

(h) as to searches in the register,

(i) as to data which, though contained in the register, is not to be—

(i) available to persons searching it, or

(ii) included in any extract issued under section 109,

(j) prescribing the configuration, formatting and content of—

(i) applications,

(ii) notices,

(iii) documents,

(iv) data,

(v) statements, and

(vi) requests,

to be used in relation to the register,

(k) as to when the register is open for—

(i) registration, and

(ii) searches,

(l) requiring there to be entered in the statutory pledges record or in the archive record such data as may be specified in the rules, or

(m) regarding other matters in relation to registration under this Part, being matters for which the Scottish Ministers consider it necessary or expedient to provide in order to give full effect to the purposes of this Part.

(2) Before making RSP Rules the Scottish Ministers must consult the Keeper.

NOTE

This section sets out that the Scottish Ministers may, by regulations, make rules (RSP Rules) providing for the operation of the Register of Statutory Pledges. They must consult the Keeper before doing so.

The power to make RSP Rules includes the powers in paragraphs (f), (g) and (i) of subsection (1) to authorise the redaction of information or signatures from an entry in the RSP, or to make certain information unavailable to searchers (which might include an individual's date of birth).

See paragraphs 35.37 and 35.38 of the Report.

CHAPTER 3

MISCELLANEOUS AND INTERPRETATION OF PART 2

Miscellaneous

115 Competence of creating an agricultural charge

On the coming into force of this section it ceases to be competent to create an agricultural charge ("agricultural charge" having the meaning given to that expression by section 5 of the Agricultural Credits (Scotland) Act 1929).

NOTE

This section prevents the creation of a new agricultural charge, which is a form of security right which is little used in practice.

See in general Chapter 38 of the Report.

Interpretation of Part 2

116 Interpretation of Part 2

(1) In this Part (except where the context otherwise requires)—

"amendment document" has the meaning given to that expression by section 60(1),

"the archive record" is to be construed in accordance with section 90,

"authorised person" is to be construed in accordance with sections 71(9) and 72(6),

"collateral-taker" has the same meaning as in regulation 3 of the Financial Collateral Arrangements (No.2) Regulations 2003 (S.I. 2003/3226)),

"corporeal moveable property" does not include money,

"encumbered property" is to be construed in accordance with section 44(3),

"financial instrument" is to be construed in accordance with the definition of "financial instruments" in regulation 3(1) of the Financial Collateral Arrangements (No.2) Regulations 2003 (S.I. 2003/3226)),

"money" has the meaning given to that expression by section 175(1) of the Bankruptcy and Diligence etc. (Scotland) Act 2007,

"provider"—

(a) is to be construed in accordance with section 43(5)(b),

(b) without prejudice to the generality of the expression, may consist of two or more co-providers, and

(c) includes any successor in title, or representative, of a provider (unless the successor or representative is a person who, by virtue of Chapter 1 of this Part, had acquired the encumbered property unencumbered by the statutory pledge in question),

"the register" is to be construed in accordance with section 87(2),

"RSP Rules" has the meaning given to that expression by section 114(1),

"secured creditor"—

(a) is to be construed in accordance with section 43(5)(a),

(b) without prejudice to the generality of the expression, may consist of two or more co-secured creditors, and

(c) includes any successor in title, or representative, of a secured creditor,

"statutory pledge" has the meaning given to that expression by section 43(4), and

"the statutory pledges record" is to be construed in accordance with section 89(2).

(2) In this Part, "right in security" (except where the context otherwise requires)—

(a) means a right in security over property and includes a floating charge, but

(b) does not include a right to execute diligence.

(3) Any reference in this Part to the "proper name" of a person is to that person's name in the form determined in accordance with rules under section 114(1)(c)(i).

(4) There is an "inaccuracy" in the statutory pledges record where that record misstates what the position is, in law or in fact, as regards a statutory pledge.

NOTE

This section defines key terms used in this Part.

Subsection (2) defines "right in security" so that it does not include, unless the context requires otherwise, a right to use diligence (the Scots law term for the several methods of enforcing a debt due under a court order (or equivalent)). The effect is that an effectively executed diligence is not to be treated as a security right for the purposes of the Part.

A "right in security" does include, unless the context requires otherwise, a floating charge.

The expression "right in security" can be used in various legal senses, including being limited to "true" securities where the secured creditor has a subordinate real right in the asset. For floating charges, however, there is no such real right prior to attachment (crystallisation) of the charge as a result of the insolvency of the legal person who granted the charge.

See paragraph 21.6 of the Report as regards a pledge over money, and paragraph 19.15 of the Report as regards the provider and the secured creditor.

117 References in Part 2 to "registering"

Any reference (however expressed) in this Part to registering—

(a) a statutory pledge, is to be construed as a reference to the Keeper's carrying out the duties imposed on the Keeper by sections 89 and 91,

(b) an amendment to a statutory pledge, is to be construed as a reference to the Keeper's carrying out the duties imposed on the Keeper by section 92(2) and (4).

PART 3

INTERPRETATION OF THIS ACT AND GENERAL

Interpretation of this Act

118 Interpretation of this Act

(1) In this Act (except where the context otherwise requires)—

"authenticated" is to be construed in accordance with section 9B(2) of the Requirements of Writing (Scotland) Act 1995,

"court" means Court of Session or sheriff,

"executed" means subscribed as a traditional document in compliance with section 2(1) of the Requirements of Writing (Scotland) Act 1995,

"the Keeper" means the Keeper of the Registers of Scotland,

"prescribed" means prescribed by regulations made by the Scottish Ministers, and

"registration number" means a unique identifier consisting of numerals or of letters and numerals.

(2) Any reference in this Act to—

(a) a "written agreement" (or to an agreement's being set out "in writing") is to an agreement,

(b) a "written confirmation" is to a confirmation,

(c) "written consent" is to consent, or

(d) a "written statement" is to a statement,

set out either in a traditional document or in a document created as an electronic communication.

(3) In subsection (2), "electronic communication" has the same meaning as in the Electronic Communications Act 2000.

(4) Where, under or by virtue of a provision of this Act, however expressed, a person (in this subsection referred to as "P") may or must proceed in some way, the provision is to be construed as if any reference in it to P includes a reference to any person authorised by P to proceed in such a way on P's behalf.

(5) The Scottish Ministers may by regulations modify (either or both)—

(a) the definition of "authenticated" in subsection (1),

(b) the definition of "executed" in that subsection.

NOTE

This is the main interpretation provision in the Bill.

Sections 42, 116 and 117 provide for the interpretation of terms used only in Parts 1 or 2 respectively, or for the definition of terms used for the purposes of particular provisions.

See also section 120 of the Bill which provides for the effect of a reference in the Bill to a requirement for any person to be in good faith.

Only some of the terms in subsection (1) call for explanation.

The definition of "authenticated" refers to the Requirements of Writing (Scotland) Act 1995, and its requirements for execution of electronic documents. But it is also possible for the Scottish Ministers to make alternative provision.

Subsection (2) has the effect that the various types of "written" document provided for by the Bill may be in the form of a hard copy or in an electronic communication (such as an e-mail). In other words, word of mouth is insufficient.

Subsection (5) lets the Scottish Ministers prescribe a different standard for executing paper documents or authenticating electronic documents than those provided for by the Requirements of Writing (Scotland) Act 1995.

General

119 Automated computer system

(1) The Keeper may, by means of an automated computer system under the Keeper's management and control, carry out the duties imposed on the Keeper under Chapter 2 of Part 1 and Chapter 2 of Part 2 of this Act.

(2) Without prejudice to the generality of subsection (1), the Keeper may, under that subsection, enable—

(a) the electronic generation and communication of applications under this Act,

(b) automated registration under this Act, and

(c) the creation of electronic documents (as defined in section 9A of the Requirements of Writing (Scotland) Act 1995).

(3) The Keeper may impose reasonable conditions for using any computer system provided for the purposes of subsection (1).

NOTE

This section authorises the Keeper to operate the Registers provided for under this Act by means of an automated computer system.

The effect is to facilitate the operation of an all-electronic register. See in that respect paragraphs 6.38 and 6.39, 6.40 to 6.45, and 29.22 and 29.23 of the Report.

120 Good faith

(1) Subsection (2) applies as respects any provision made in this Act as respects good faith.

(2) If there is a dispute as to whether a person was in (or acted in) good faith, the burden of proof lies on whoever asserts that the person was not in (or did not act in) good faith.

NOTE

This is a general provision relating to good faith provisions in, for example, sections 11 and 12 of the Bill.

The effect is that, where an issue arises as to whether or a person is in good faith for the purposes of a provision in the Bill, then it is for the person asserting a lack of good faith to prove that the person was not in good faith.

121 Ancillary provision

(1) The Scottish Ministers may by regulations make such incidental, supplementary, consequential, transitory, transitional or saving provision as they consider appropriate for the purposes of, or in consequence of, or for giving full effect to, any provision made by, under or by virtue of this Act.

(2) Regulations under subsection (1) may modify any enactment (including this Act).

NOTE

This section provides for a general regulation-making power, that enables the Scottish Ministers to make provision for consequential and other incidental matters in order to give full effect to the Bill.

The power in this section allows the Scottish Ministers to amend any enactment including the Bill, and any regulations that do so will be subject to affirmative procedure (see section 122 of the Bill).

For the meaning of "enactment" see schedule 1 of the Interpretation and Legislative Reform (Scotland) Act 2010.

122 Regulations

(1) Regulations under section 3(6), 5(7), 36(2)(b)(i), 47(2)(d), 51(4), 52(3), 53(5), 55(1)(a), 99(1), 118(5) or (if modifying an enactment) 121(1) are subject to the affirmative procedure.

(2) Any other regulations under this Act, other than regulations under section 123(2), are subject to the negative procedure.

123 Commencement

(1) This section and sections 121, 122 and 124 come into force on the day after Royal Assent.

(2) The other provisions of this Act come into force on such day as the Scottish Ministers may by regulations appoint.

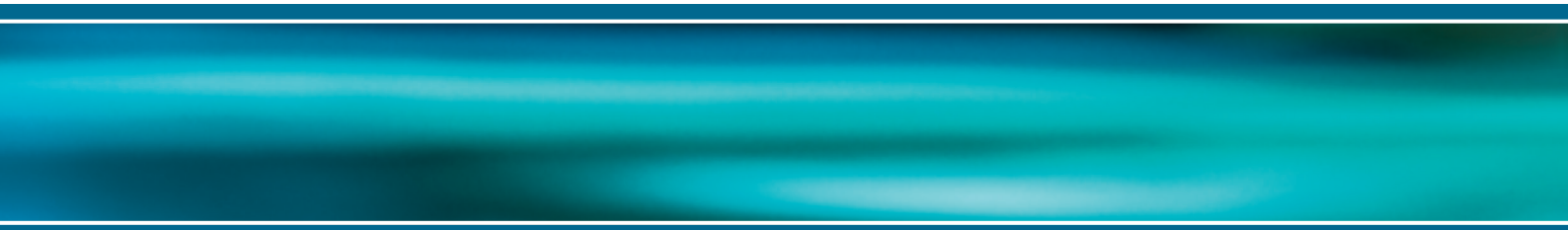
(3) Different days may, under subsection (2), be appointed for different purposes.

NOTE

The provisions in the Bill will, except as provided for here, come into force on the day or days appointed by the Scottish Ministers in regulations made for that purpose under this section.

124 Short title

The short title of this Act is the Moveable Transactions (Scotland) Act 2017.



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