Conveyancing and Feudal Reform (Scotland) Act 1970 – is it fit for purpose?

6 October 2020

Introduction

- In 1964 a committee under the chairmanship of Professor John Halliday was appointed:

  "To examine and report on existing conveyancing legislation and practice in relation to heritable and moveable property and to make recommendations with a view to amending or [introducing] new legislation."

- The committee's report was published in 1966. On the heritable security the Report states:

  "We consider that the only effective solution of the many difficulties inherent in the present forms of heritable security is to devise a new and flexible form of security, adaptable for use in connection with all kinds of advances on heritable property, which will supersede all existing forms"

Conveyancing and Feudal Reform(Scotland) Act

- The 1970 Act introduced the concept of the standard security
- Only competent way to grant heritable security
- Did not abolish existing forms of heritable security
- Includes provisions dealing with ranking, assignation, variation, discharge and enforcement
- Professor Gretton described the 1970 Act as *“one of the most important, and one of the most welcome and successful reforms of the law of security that our law has ever seen”*

Analysis

Initial observations on the Act 50 years on

Look at the challenges before the courts in the last decade

Scottish Law Commission's review

The Act – a half century on

Certain aspects have aged well - reflected in the recommendations in Scottish Law Commission's First Discussion paper

Replacing several forms of heritable security with the standard security simplified the law

Created a true security. The debtor retains ownership and the creditor only has a subordinate right in the property

The standard security also offers flexibility in relation to the debt it can secure. It can be a fixed amount or a fluctuating amount. It can be debt already owed or a debt yet to be advanced

The Act – a half century on (cont'd)

Act is starting to show its age

Overly complex

- Certain rules contained in Act others in Schedule 3
- Amendments principally the 2010 Act
- number of statutory forms

Lack of accessibility - while much of the law on heritable securities is in the 1970 Act, there are many other relevant provisions in other legislation

- Makes this key area of law less accessible than it should be
- A number of the provisions in the Act are detailed & difficult to follow

The Act – a half century on (cont'd)

Dated - reflects an era when economic activity was less sophisticated:

- Growth & interconnectivity of the financial market
- Consumer/regulatory intervention
- Securitisation of loans as an investment class

Professors Reid & Gretton:

"[T]he 1970 Act . . . is fussy and over-prescriptive. The styles in the schedules can be difficult to follow faithfully. The Scottish Law Commission is embarking on a review of the law of heritable security, and it may be hoped that the eventual result will be a certain degree of defussification (we just made this word up) of the legislation."

What has precipitated change?

"Events, dear boy, events" Harold Macmillan	2008 financial crisis	Increased consumer protection to align process in Scotland with E&W where a pre-action protocol applied for repossessions
Pre action requirements where property used for residential purposes	Home Owner and Debtor Protection (Scotland) Act 2010	Commencement date 30 September 2010

Royal Bank of Scotland plc v Wilson

Supreme Court decision issued 26 November 2010

Overruled Bank of Scotland v Millward & decades of legal practice

Without Wilson doubtful that the Law Commission would be undertaking its review of heritable securities

Tension between the Supreme Court's decision & the 2010 Act

Difficulties apparent in the number of legal challenges lenders have faced in enforcing their rights over the last decade

Meaning of Default

- Northern Rock (Asset Management) plc v Millar
- Pre Action Requirements (Scotland) Order 2010 Regulation 2(4)

  "The information required to be provided to the debtor … must be provided as soon as is reasonably practicable upon the debtor entering into default."
- Sheriff Deutsch held that default in the Regulations must have the same meaning as it had in the 1970 Act and default arose on expiry of the Calling Up Notice
- Tortured approach – PAR completed before and after the legal process has commenced
- Confusing and opaque process

Used for residential purposes

- Section 20(2A) 1970 Act

  "Where the standard security is over land or a real right in land used to any extent for residential purposes, the creditor is entitled to exercise the rights specified in standard condition 10(2) and (3)… only –

  a) where the conditions in section 23A of this Act are satisfied, or

  b) with the warrant of the court, granted on an application under section 24 of this Act"

- Westfoot Investments Limited v European Property Holdings Incorporated 2015 SLT (Sh Ct) 201

- Royal Bank of Scotland plc v Mirza [2017] SAC (Civ) 13

Westfoot Investments Limited v European Property Holdings Incorporated

Westfoot advanced short term loan for 6 months secured over two residential properties in Edinburgh. Loan called up and Westfoot raised proceedings to enter into possession and sell the properties

It was conceded by the pursuer that the protections afforded by the 2010 Act were engaged despite the debtor being a Panamanian property development company

Sheriff disagreed & adopted a purposive interpretation of the 2010 Act in finding that the securities were not over land used to any extent for residential purposes

"However property used for residential purposes, is property used as a home. But whose home?...it must be a home used either by the grantor of the security subjects or the maker of the obligation secured."

Westfoot Investments (cont'd)

"In my opinion the sole beneficiaries of the legislation are debtors who own their home and use it as a security for debt, home owners who allow the home they mostly live in to be used as security for someone else's debt, occupiers whose home is not otherwise protected by legislation and entitled residents [including, for example, estranged partners of debtors] who live solely or mainly in a home used by a debtor or proprietor to secure a debt"

"However, corporate borrowers that grant standard securities over their residential property assets and use these as collateral security, to raise capital on the financial markets, are not included within the scope of the protection created. That kind of borrowing is a commercial activity"

Royal Bank of Scotland plc v Mirza

Pursuer granted decree entitling it to enter into possession and sell a residential property

The defender did not occupy the property when the calling up notice was served or expired

Question of whether the property was land used to any extent for residential purposes was considered by the Sheriff Appeal Court

In refusing the appeal the SAC adopting a different approach to that of the sheriff in Westfoot

RBS v Mirza (cont'd)

"The kernel of the reasoning of the sheriff in Westfoot Investments on this point is located in paragraph 24 of his judgment, where he states: "However, property used for residential purposes, is property used as a home. But whose home?... It must be a home used either by the grantor of the standard security or the maker of the obligation secured." We would put the matter in a slightly different way. The mischief addressed by the 2010 Act and 2010 Order is to give greater protection to such occupiers of security subjects. However, when one has regard to the scope and nature of the protective regime that is enacted, it is clear that not every occupier has the benefit of that regime. Since section 24(1B) is the process by which the protective regime is initiated, it follows that one requires to construe the applicability of the regime having regard to those persons intended to benefit by it…

Mirza (cont'd)

The clause "land used to any extent for residential purposes" admits in our view of a rather different and antecedent purpose to that posed by the sheriff in Westfoot Investments. The question is simply this: "Were the subjects, to any extent, used for residential purposes? That must always be a question of fact. In our view the word "residential" qualifies the purpose rather than the property referred to in the clause. It follows that in certain circumstances security subjects may be occupied or unoccupied and yet remain residential in the sense that we have described. Factual presence in a property may not be a determinative factor. Temporary absence can and should be accommodated within the definition. The examples of a resident in a hospital or a hospice were helpfully raised in discussion before us"

Assignations – One Savings Bank v Burns

OSB having acquired by assignation title in a standard security sought to take possession of the property

The assignation was recorded in the General Register of Sasine

The borrower successfully challenged the validity of the assignation

Sheriff Mann concluded that it did not conform to the required statutory form, as it did not specify the outstanding sum at the time the standard security was assigned

Shear v Clipper Holdings

Application for interim interdict by borrower seeking to prevent a creditor, which had acquired its title by assignation, from enforcing its rights

The assignation was in similar terms to the style used in the OSB case and was registered in the Land Register

The borrower relied on the decision in OSB in contending that the creditor did not have title to enforce the rights provided by the standard security

Lord Bannatyne refused to grant interim interdict

Shear v Clipper Holdings (cont'd)

Following OSB would not have given effect to the statutory purpose of an assignation as provided in section 14 of the 1970 Act & would result in an unjust outcome

Lord Bannatyne's reasoning shows the court's willingness to apply an interpretation that makes commercial sense and achieves a fair outcome

Lord Bannatyne was sitting alone as a judge at first instance

Both decisions are persuasive and not binding upon other courts. The decision in Clipper is nevertheless a decision of a Lord Ordinary sitting in the Court of Session and is likely to be more persuasive than the decision in OSB

Promontoria v The Firm of Portico Holdings

The debt was secured by thirty four all sums due standard securities assigned to Promontoria

There were no balance figures in the assignation which contained the phrase: *“to the extent of all obligations and liabilities due or to become due by the relevant Chargor to the Buyer”*

The parties and security subjects were set out in the assignation

The calling up notice(s) which Promontoria issued included the outstanding balance

Promontoria (cont'd)

Promontoria enforced the standard securities and the borrowers challenged the validity of the assignation

The borrowers contended that the assignation was invalid because it did not state the outstanding balance

It was accepted there was no substantive defence to the claim

Promontoria contended that the assignation was valid as the wording used kept the assignation "*as closely as may be*" to the statutory Form A.

Alternatively, if the assignation was not strictly compliant with the legislation any omission was not fatal

Promontoria (cont'd)

The sheriff followed Shear v Clipper Holdings and found the assignation to be valid

In the circumstances of the case the form of wording used was wholly reasonable and was "as close as may be" to the statutory style

The sheriff went further and said that even if he had found the assignation to be non-compliant with the statutory form, any variation was not fatal as it caused no prejudice

The borrowers should not be able to rely on what was a technical challenge as a means to delay repayment

Scottish Law Commission

- Review began 2018 - expected to run for up to 5 years
- Expert advisory group which has met three times
- Two Discussion Papers proposed:

The first paper considers pre-default matters such as the creation and transfer of heritable securities and the obligations which they can secure

The second paper will deal with post-default matters and how heritable securities are enforced

A single Report and draft Bill will be published in due course

Discussion Paper 1: Pre-default

Published on 18 June 2019, and consulted on 61 proposals or questions. Consultation closed on 30 September 2019

Aim to clarify and consolidate the current law, and to provide more flexible ways to create and deal with a standard security

Proposes to keep the name ‘standard security’, that the standard security should continue to be the only form of heritable security that can be granted, and that current enactments (including the 1970 Act) should be replaced by a new Act.

Discussion Paper 1: Pre-default (cont'd)

Proposes there should no longer be statutory forms for security documents, and that instead the law should set out requirements to be met by (for example) the constitutive document of a standard security

Asks whether there should be any restrictions on what all-sums securities may secure, and in particular whether the security should cover pre-assignation debts owed to the assignee or debts originally owed to other parties

Asks whether a new Act should provide a freely available default set of standard conditions for use for example by non-commercial lenders

Discussion Paper 1: Pre-default (cont'd)

Preliminary view is that the monetary element of any claim relating to a non-monetary obligation should be able to be secured by a standard security, but nothing else. This follows from the fact that the methods for enforcing a security are designed to raise money

Proposes that the effect of an assignation should not limit the security to the amount due to the then current security holder at the date of assignation, and that future advances made by the assignee should be capable of being secured

Asks whether a new Act should provide a freely available default set of standard conditions for use for example by non-commercial lenders

Post default & enforcement

Some preliminary work carried out to date on enforcement

The Advisory Group and other interested parties asked to comment on issues raised by this part of the project

Dr John MacLeod of the University of Edinburgh, has prepared a research paper on enforcement of heritable securities

In the paper, Dr MacLeod describes and analyses the law in England and Wales, France, Germany, New Zealand and South Africa, with a view to finding models which can be drawn upon

The Commission expects to make substantial use of the paper during the second part of this project

Post default & enforcement (cont'd)

Non exhaustive list of issues raised by stakeholders:

The rules on enforcement are too complex and should be simplified

Residential property is protected, but it is not always clear what is or is not residential, and it might be better to protect specified persons

The rules for service on dissolved companies are inconsistent, and service on the Lord Advocate should be competent in all such cases

The rules on service on representatives in circumstances other than death, particularly incapacity, need to be clarified

The rules on when pre-action documents must be served should be clarified

Post default & enforcement (cont'd)

The rules on which parties must consent to a voluntary surrender of empty residential property should be reviewed

The meaning of "unoccupied" should be clarified, for example, its application to holiday homes

The meanings of "entering into possession" and "in lawful possession" as used in the 1970 Act need to be clarified

The expenses to which a creditor is entitled under standard condition 12 of the 1970 Act should be examined

The rule by which an enforcement decree does not prescribe for 20 years should be reviewed given that other enforcement rights prescribe after 5 years under the 1970

Conclusion

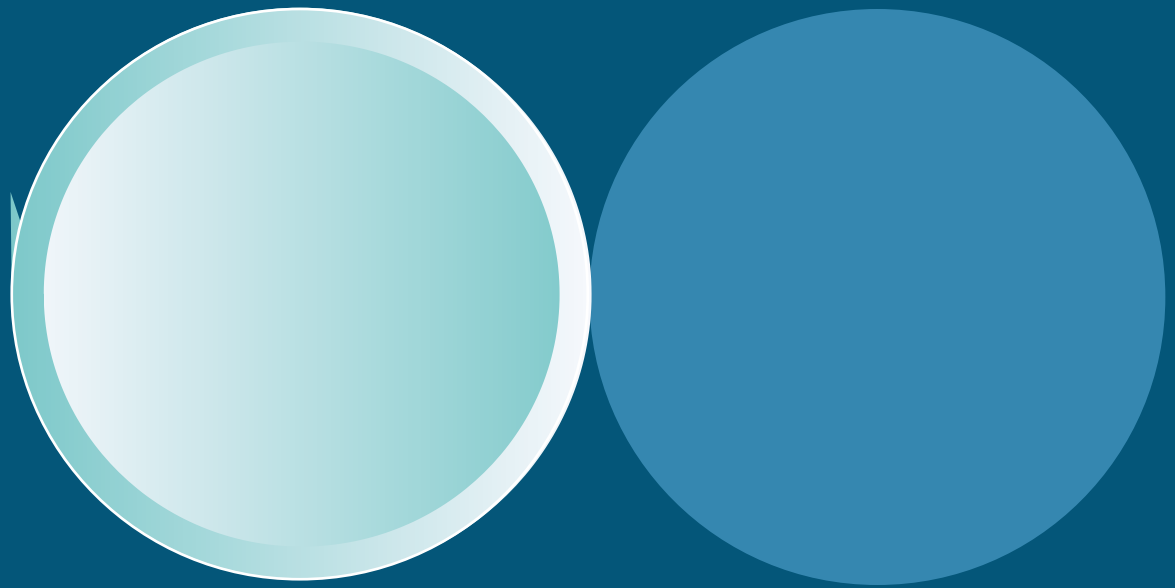
Answer to question posed at outset hopefully apparent

1970 Act clearly not fit for purpose from a litigation perspective

SLC'S Second discussion paper will contain a number of proposals to address the many concerns raised

Report & Bill some time away – possibly another 2/3 years

Deliver simplified and more accessible framework for enforcement to bring clarity to the opaque environment in which we are currently operating



Questions?

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