
# FACULTY OF ADVOCATES

**RESPONSE**

**FROM**

**THE FACULTY OF ADVOCATES**

**TO**

**CONSULTATION ON THE**

**DISCUSSION PAPER ON HERITABLE SECURITIES: DEFAULT AND POST DEFAULT**


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# Summary of Proposals

1. What information or data do consultees have on:

   (a) the economic impact of the current legislation on heritable securities, or

   (b) the potential economic impact of any option for reform proposed in this Discussion Paper?

(Paragraph 1.22)

**Comments on Proposal 1**

The Faculty of Advocates does not have information or data to make available.

2. When exercising a standard security, should a security holder be subject to a duty to conform with reasonable standards of commercial practice?

(Paragraph 2.29)

**Comments on Proposal 2**

While this is an issue of policy, we consider that there should be a duty to conform with reasonable standards of commercial practice. It would mean that there was consistency between heritable and moveable securities. We recognise that it will add some complexity to enforcement and will impose a burden on lenders but we do not consider that, in general, that would be seen as unreasonable. One situation in which the burden might be greater is where the security holder is not a commercial lender. For example, situations arise within families and, in particular, family owned businesses where securities are granted in respect of obligations. In such situations, the security holder is unlikely to be aware of what is required by the reasonable standards of commercial practice. The issue then would be whether the existence of this limited class of situations means that the protection should not be provided generally.

Where the security holder is obliged to comply with FCA requirements it is not likely to impose additional requirements. However, where the security holder is not so obliged is likely to be the situation in which protection is most required.

It has the advantage that as the standards evolve over time so would the requirement. This will prevent the law becoming out of date. Most importantly, it will apply in those situations where the security holder is not otherwise subject to regulation. These might be thought to be the situations where the borrower is most in need of protection.

3. Do consultees have any comments on our approach to redemption post-default as outlined above?

(Paragraph 2.38)

**Comments on Proposal 3**

No comments

4. (a) Do consultees consider that any new legislation should make provision regarding the enforcement of *ex facie* absolute dispositions?

(b) If so, what should the effect of any such provision be?

(Paragraph 2.44)

**Comments on Proposal 4**

In view of the limited number of *ex facie* absolute dispositions in security, the resource implications in preparing new legislation and the fact that there is an established set of legal rules on such securities (albeit old), we consider that there should not be provision in new legislation for enforcing these securities.

5. Should new legislation restate the principle *prior tempore, potior jure* as it applies to security over heritable property?

(Paragraph 3.24)

**Comments on Proposal 5**

For reasons of maintaining consistency, the principle should be left to the general law.

6. (a) Should a subsequent standard security holder be able to restrict the priority of an earlier standard security by giving notice?

(b) If so, should post-notice voluntary advances by the prior security holder be unsecured, or treated in some other way?

(Paragraph 3.32)

**Comments on Proposal 6**

Legislation should continue to make provision for a subsequent security holder to restrict the priority of an earlier standard security by giving notice. If this is not done, the existence of an all-sums security would mean that the debtor would in practice be unable to borrow against remaining equity in the subjects of the security. As part of the purpose of securities is that a person owning property should be able to exploit its value to obtain borrowings which may provide economic and/or personal advantage, it is desirable that this portion of equity should not be 'sterilised'.

It is accepted that the effect of the ability to give notice will probably be taken away in many

cases by agreement between the parties. That, however, is simply part of freedom of contract. Changing the law would remove even the possibility of being able to use the property for further security. In the current situation there is at least some element of choice and taking away the ability to restrict would remove that choice.

What is principally required in relation to post-notice voluntary advances by the first security holder is clarity as to the legal position. The preferable outcome would be that the further advances be unsecured. If that was not acceptable, either no advance would be made or a further security could be granted and intimation could be given to the second-ranked security holder. The alternative of postponing the first security holder's advances to those of the second security holder may lead to uncertainties when postponed securities are granted to more than one party.

7. Do consultees agree that:

(a) The parties to a standard security and any other right in security should be free to enter into a ranking agreement intended to vary the terms of the security?

(b) Such agreements must be set out in writing?

(c) Registration of the agreement in the Land Register is required to vary the terms of the standard securities concerned?

(Paragraph 3.36)

**Comments on Proposal 7**

We agree with all three propositions.

8. A security holder may exercise remedies under a standard security where:

(a) there is a failure to perform the secured obligation; or

(b) in such other circumstances, if any, as are agreed between the debtor, the owner or registered tenant of the security property, and the security holder.

Do consultees agree?

(Paragraph 4.47)

**Comments on Proposal 8**

We agree with the proposition.

9. (a) Should new legislation specify circumstances in which a security holder may exercise remedies under a standard security beyond those listed in question 8 above?

(b) If so, which circumstances should be specified in the legislation?

(c) Should the specified circumstances be subject to variation by the parties to the security?

(Paragraph 4.50)

**Comments on Proposal 9**

We note that views are not sought on the proposal that the legislation should not specify what will amount to a failure to perform the secured obligation. Nonetheless, we suggest that "failure to perform" is a vague test and not one used elsewhere. We consider that it would be better to frame it as being when there is a breach of any of the secured obligations.

We agree that legislation should not specify other circumstances in which the security holder may exercise remedies. If they must be contained in the agreement between the parties, it is more probable that they will come to the attention of the debtor and it is appropriate to have them contained in one place as opposed to several.

10. Do consultees agree with the proposal that:

(a) Prior to exercising remedies under a standard security, the security holder will be required to serve a notice known as a default notice?

(b) The security holder will not be entitled to exercise remedies unless and until the default notice expires?

(Paragraph 5.11)

**Comments on Proposal 10**

(a) We agree that a notice should continue to be required. We also agree with the suggestion made in the Discussion Paper that a single notice (rather than separate Notices of Default and Calling-Up Notices) should be utilised. The unclear distinction between the two forms of notice has caused difficulties in practice and should not be retained.

(b) We agree with this proposal.

11. Do consultees agree that the form of the default notice should be prescribed by legislation?

(Paragraph 5.15)

**Comments on Proposal 11**

We agree that the form should be prescribed by legislation, and note that this approach is consistent with the approach to other forms of notice (including those presently required under the 1970 Act).

We are aware that practical issues have sometimes been caused by the use of the same form of notice for residential and non-residential properties. This is because the form contains information which is applicable only to residential properties and the separate protection for which they qualify. Consideration might be given to using different forms for properties which qualify for this protection and those which do not.

12. (a) Should the form of the default notice be prescribed in primary or secondary legislation?

(b) What comments do consultees have on the suggested list of key information to be included in the default notice?

(c) What further key information, if any, should be included?

(Paragraph 5.18)

**Comments on Proposal 12**

(a) We agree with the analysis in the discussion paper (at para 5.16) that secondary legislation is likely to offer more flexibility but primary legislation will offer greater accessibility to debtors. The balance between these two considerations is essentially a matter of policy, upon which we have no further comments.

(b) We agree with inclusion of the items on the proposed list.

(c) It may assist the aim of accessibility if the default notice is also required to stipulate the statutory provision(s) in terms of which it proceeds. Given that default notices are likely to be served principally by agents rather than by creditors directly, it might also assist debtors if the notice required the details of the agent (and the means by which they can be contacted) to be clearly stated where applicable.

13. Do consultees agree with the proposal that a default notice may be served by the security holder or its agent?

(Paragraph 5.20)

**Comments on Proposal 13**

We agree with this proposal which appears to us to be essential to the practical operation of the legislation.

We note that the proposal in the Discussion Paper – 'creditor or its agent' – is slightly narrower than the present statutory wording, which also gives the right to serve a notice to successors, assignees and representatives of the creditor. We are not aware that this wider category has caused any difficulties in practice, and suggest that it should be retained (not least because its removal might cause doubts as to the position of parties who are not the original creditor, such as assignees).

14. Do consultees agree with the following provisional proposals?

(a) A default notice must be served on the debtor, the owner or registered tenant of the security property, and any other person against whom the security holder wishes to preserve a right of recourse in respect of the secured obligation.

(b) Where a natural person on whom service should be made is deceased, service must instead be made on any person appearing from the title to have succeeded to the security property, or on the confirmed executor of the deceased estate. If no successor appears on the title and no executor has been confirmed, service must be made on the Lord Advocate.

(c) Where a natural person on whom service must be made has been sequestrated, service must also be made on the trustee in sequestration (unless discharged).

(d) Where service is to be made on a body of trustees, it is sufficient for service to be made on the majority of trustees.

(e) Where a company on which service should be made has been removed from the Register of Companies, service should be made on the Lord Advocate.

(f) Where the address of the person upon whom service should be made is unknown, or it is unknown whether the person is alive, or the notice is returned with intimation that delivery was unsuccessful, service is to be made on the Extractor of the Court of Session.

(Paragraph 5.29)

**Comments on Proposal 14**

We agree with the categories of person identified upon whom notice should be served and (subject to our comments below) with the means by which that should be effected.

In relation to category (b) (deceased persons) we consider that it is desirable that (as the Discussion Paper proposes) the category of 'representative' of the deceased be clarified. We consider, however, that the drawing of this category to extend only to those benefiting from survivorship destinations and confirmed executors may be too narrow. In particular, it is our experience in practice that in smaller estates, confirmation is not always obtained (notwithstanding that this should be done where heritable property is involved). The drawing of the category to include only confirmed executors has the potential to exclude the necessity for service on this class of estate.

15. Where a security holder has been made aware that a guardian or attorney is acting on behalf of an intended recipient of a default notice who is an adult with incapacity, should service be made solely on the guardian or attorney on that adult's behalf?

(Paragraph 5.31)

**Comments on Proposal 15**

The question of whether it is desirable to avoid service upon adults with incapacity is essentially one of policy, upon which we have no comments.

With reference to the suggestion that service should be made solely on the guardian or attorney, we note that this may give rise to practical issues and uncertainty. This is because capacity and incapacity may not be (and typically is not) binary. The standard against which 'incapacity' for the purposes of service would require to be assessed would need to be defined in order for a creditor to be certain that notice had been served correctly. Moreover, a creditor is unlikely to be in possession of sufficient information to make a properly informed judgment as to capacity.

16. Should it be competent to serve a default notice by:

(a) Sheriff officer, using the methods specified in the Ordinary Cause Rules 1993, rule 5 (namely delivery into the hands of a recipient who is a natural person; leaving the notice in the hands of a resident at the recipient's dwelling or in the hands of an employee at the recipient's place of business; letterbox delivery following diligent enquiry; or leaving the notice at the recipient's dwelling place or place of business in such a way that it is likely to come to their attention following diligent enquiry)?

(b) Sending it to the intended recipient by a postal service which provides for delivery of the notice to be recorded?

(c) Electronic transmission where the electronic form of the notice and the electronic address for service has been agreed in writing by all relevant parties in advance?

(Paragraph 5.40)

**Comments on Proposal 16**

We agree with proposals (a) and (b). In relation to proposal (c), we note that electronic service may give rise to difficulties for debtors if an agreed address for service is not regularly monitored (one example would be an email address agreed some years previously when the security was originally granted, and which is no longer active or monitored; such problems are rather more likely to result in relation to individual email accounts than corporate ones). Electronic service is likely to bring practical benefits in many cases, but we suggest that provision is made either for agreement to be recent in relation to the date of service, or for confirmation that a message has been received and read to be required.

17. Which, if any, other methods of service should be competent for default notices?

(Paragraph 5.41)

**Comments on Proposal 17**

We are not aware of any other methods.

18. Should relevant parties be permitted to agree in writing, prior to service of a default notice, that it must be served:

(a) By one (or more than one) of the methods specified in the statute?

(b) At a specified address?

(Paragraph 5.43)

**Comments on Proposal 18**

We agree with this proposal.

19. Should the time limit for compliance with a default notice be:

(a) 14 days after service?

(b) One month after service?

(c) Two months after service?

(d) Some other period, and if so, what?

(Paragraph 5.46)

**Comments on Proposal 19**

This question is one of policy, upon which we have no comments.

20. Do consultees agree that the time limit for compliance with a default notice may be varied or dispensed with following service of the notice where consent is given in writing by all the following parties:

(a) the debtor;

(b) the owner or registered tenant;

(c) holders of any prior or *pari passu* securities;

(d) the spouse of the debtor, owner or registered tenant where the security property is a "matrimonial home" in terms of the Matrimonial Homes (Family Protection) (Scotland) Act 1981 s 22;

(e) the civil partner of the debtor, owner or registered tenant where the security property is a "family home" in terms of the Civil Partnership Act 2004 s 135(1);

(e) any "entitled resident" of the security property as defined in the enhanced debtor protection provisions of any new standard securities legislation?

(Paragraph 5.48)

**Comments on Proposal 20**

This question is one of policy, upon which we have no comments.

21. Should section 21 of the Interpretation and Legislative Reform (Scotland) Act 2010 be excluded from application to any new standard securities legislation, and if so, why?

(Paragraph 5.54)

**Comments on Proposal 21**

We consider that it is desirable that section 21 should apply to the legislation. Section 21 states a principle of general application, and we are not aware of any reason why notices under the Act should be treated in a different fashion. We also consider that there are benefits to utilising a provision in general use and which has already been considered by the

courts.

22. Should a bespoke route of challenge to a default notice (similar to that found in section 22 of the 1970 Act) be provided for in any new legislation?

(Paragraph 5.59)

**Comments on Proposal 22**

We agree that a bespoke route of challenge should be provided. A bespoke route of challenge is likely to be more appropriate in terms of accessibility. It also acknowledges the expertise of the Sheriff Court in dealing with matters relating to the enforcement of heritable securities.

23. (a) After what period of time should the rights of a security holder to exercise remedies on the basis of an expired default notice be extinguished by prescription?

(b) Why?

(Paragraph 5.64)

**Comments on Proposal 23**

This question is one of policy, upon which we have no comments.

24. Should an expired default notice continue to provide a valid basis for the exercise of remedies where the default giving rise to the notice is subsequently purged? Why or Why not?

(Paragraph 5.68)

**Comments on Proposal 24**

This question is one of policy, upon which we have no comments.

25. Do consultees agree that a court order should not be required to exercise a remedy under a standard security, except where legislation specifically so provides?

(Paragraph 6.20)

**Comments on Proposal 25**

We agree.

26. Should a security holder be able to apply to the court for relevant orders in relation to the exercise of remedies even where such an order is not required by legislation?

(Paragraph 6.21)

**Comments on Proposal 26**

We agree that this possibility should be open.

27. Should court proceedings in respect of the exercise of standard securities be raised by way of ordinary cause procedure, except in cases to which the enhanced debtor protection measures apply?

(Paragraph 6.23)

**Comments on Proposal 27**

There does not appear to be any reason to innovate on the current position.

28. (a) Should the obligation to obtemper a decree of court obtained under legislation on standard securities continue to be subject to the long 20-year prescription?

(b) If not, why not?

(Paragraph 6.27)

**Comments on Proposal 28**

The twenty year prescriptive period should continue to apply. We are not aware of any suggestion that decrees are obtained and "held over the debtor's head". It is not desirable to distinguish decrees of Courts in this respect from any other decrees.

29. Should the person criterion for application of the enhanced debtor protection measures be satisfied where both the debtor and the owner of the security property are natural persons (including where the debtor and owner are the same person)? If not, what difficulties do you identify with this proposal?

(Paragraph 7.55)

**Comments on Proposal 29**

We consider that the approach of applying the enhanced debtor protection measures where either the debtor or the owner is a natural person is preferable. This will remove cases where the debtor and the owner are both juristic persons.

30. Where the debtor is a natural person and the owner of the security property is a juristic person, should any of the enhanced debtor protection measures be disapplied or otherwise modified? If so, which measures should be disapplied, or which modifications should be made?

(Paragraph 7.55)

**Comments on Proposal 30**

We recognise that there may be arguments for disapplying or modifying the protections in these circumstances. However, we consider that others would be better placed to comment on these matters.

31. Where the debtor is a juristic person and the owner of the security property is a natural person, should any of the enhanced debtor protection measures be disapplied or otherwise modified? If so, which measures should be disapplied, or which modifications should be made?

(Paragraph 7.55)

**Comments on Proposal 31**

We consider that disapplying any of the measures where the owner of the security property is a natural person would be inconsistent with the policy intentions of the PARS.

Many individuals choose to operate their businesses through companies. Where they do so, they will often be asked to provide personal guarantees for the liabilities incurred by the company. Those personal guarantees will often be secured by a standard security over the individual's family home. The policy intentions identified in the Consultation Paper would apply equally to those individuals as it would to those whose liabilities arise from debts incurred as a sole trader.

32. (a) Should the property criterion for application of the enhanced debtor protection measures be satisfied where the security property comprises or includes a dwellinghouse?

(b) If not, what difficulties do you identify with this proposal, and what would you propose as an alternative?

(Paragraph 7.62)

**Comments on Proposal 32**

We agree that the proposed wording is in keeping with the policy intention behind the provisions.

An example of a potential difficulty with this proposal is where a large area of development land includes a dwellinghouse which may or may not be occupied. On the proposed definition, the enhanced debtor protection measures would apply. However, the enhanced debtor protection measures would already apply in these circumstances under the current regime. We have been unable to identify any way of removing examples of this type from the scope of the measures without creating other difficulties. We consider that a more expansive approach is more in keeping with the intention of Parliament than one which risks removing properties that are used as dwellinghouses from the protections of the provision.

33. Should the term "dwellinghouse" be defined in new legislation, if the property criterion is that the security property "comprises or includes a dwellinghouse" as suggested above?

(Paragraph 7.62)

**Comments on Proposal 33**

We consider that the term "dwellinghouse" should be defined in new legislation. That will ensure that the meaning of that term is not open to dispute.

34. (a) Should buy-to-let properties be excluded from the application of the enhanced debtor protection measures?

(b) Should the legislation provide for any other exceptions, and if so, what?

(Paragraph 7.62)

**Comments on Proposal 34**

We agree with the views expressed by the Commission. Whilst there is an argument for excluding buy-to-let properties, doing so would make the procedure more complex. Properties which are bought as a debtor's residence may subsequently be let out. Whilst loan agreements will usually require a lender's consent for this to occur, this will sometimes occur without the lender's consent or knowledge. We agree that a test that can be applied without undertaking investigations as to the actual occupation of the property is preferable.

35. Where a default notice is served in relation to a security property which meets the property criterion for application of the enhanced debtor protection measures, the security holder must give notification of the same to the occupier(s) of that property and to the local authority in which the property is located.

Do consultees agree?

(Paragraph 7.67)

**Comments on Proposal 35**

Yes. This is not an onerous requirement. It is one with which security holders and their advisers are already familiar.

36. Are any amendments, additions or deletions to the PARs required? If so, what?

(Paragraph 8.6)

**Comments on Proposal 36**

We consider this question to raise matters of policy and practice on which others would be better placed to comment.

37. Should the "headline" requirements of the PARs continue to be provided for in primary legislation, with further detail in secondary legislation and guidance, as at present?

(Paragraph 8.7)

**Comments on Proposal 37**

We agree with this proposal. It is important in this area of law that individuals and their advisers are able to access the law easily. We consider that what is proposed offers an appropriate means of doing this.

38. Other than those outlined in this Discussion Paper, what difficulties exist with the procedure for application for warrant under the 1970 Act, section 24(1B)?

(Paragraph 8.10)

**Comments on Proposal 38**

We consider this question to raise matters of policy and practice on which others would be better placed to comment.

39. (a) Should new legislation continue to provide a non-exhaustive list of factors to be taken into account by the court when determining an application for warrant to exercise remedies where the debtor appears or is represented, modelled on the current section 24(7)?

(b) Should the final factor listed in section 24(7) be amended in new legislation to restrict the court's consideration to the ability of the debtor, the owner, any entitled

resident and any child of the foregoing parties residing with them to find reasonable alternative accommodation?

(c) Are any other amendments, additions or deletions to the section 24(7) factors required? If so, what?

(Paragraph 8.14)

**Comments on Proposal 39**

We consider that a non-exhaustive list is helpful in identifying the types of factor which will be relevant in the exercise of the Court's discretion.

We agree that the proposed revisal is consistent with the policy intention behind the provision. We can see benefit in the clarification proposed.

We have no other amendments, additions or deletions to propose.

40. Should new legislation provide the court with guidance on how to balance the interests of the debtor, owner and entitled residents in considering factors equivalent to those currently listed at section 24(7)? If so, what guidance should be given?

(Paragraph 8.15)

**Comments on Proposal 40**

We do not consider that there is a need for further guidance to be given on this issue. Each case is likely to be fact specific. It is difficult to see how any guidance could usefully be given without it becoming too detailed and prescriptive. We consider that it would be preferable to allow these matters to be addressed by the Court as and when they arise.

41. Are any amendments, additions or deletions required to the definition of entitled resident set out in section 24C? If so, what?

(Paragraph 8.18)

**Comments on Proposal 41**

We consider this question to raise matters of policy and practice on which others would be better placed to comment.

42. (a) Following expiry of a default notice, should the requirement for warrant of the court under the enhanced debtor protection regime be waived where the debtor, the owner and any entitled residents confirm in writing that:

(i) they are not in occupation of the security property;

(ii) they consent to the exercise of remedies under the security;

(iii) their consent was given freely and without coercion of any kind?

(b) Should the debtor, the owner and any entitled resident also be required to confirm that the security property is unoccupied?

(Paragraph 8.22)

**Comments on Proposal 42**

In respect of question (a) we agree with the views expressed in the Consultation paper.

As regards question (b), we consider that this question raises questions of policy and practice on which others would be better placed to comment.

43. (a) Should new legislation on standard securities make available the same remedies as current legislation?

(b) Should new legislation include any remedy not currently provided for, and if so, which remedy?

(Paragraph 9.5)

**Comments on Proposal 43**

In respect of (a), our answer is Yes. In respect of (b), our answer is No. We agree with the observation in the Discussion Paper that there is no suggestion that any of the existing remedies should cease to be available nor are there any obvious remedies missing from the current statutory scheme for enforcement of a standard security.

44. Should receivership be available as a remedy under any new legislation on standard securities? If so, what powers should be available to the receiver?

(Paragraph 9.12)

**Comments on Proposal 44**

Our answer is No.

We agree with the observation that receivership is principally a feature of general insolvency law. In that context, we also note that the right of a floating charge holder to appoint an administrative receiver has been restricted since the Enterprise Act 2002 due to perceived inadequacies of that system in rescuing companies and/or producing a better return for creditors than liquidation. Standing the fact that receivership would appear to add little or nothing to the existing remedies available under Scots law, we cannot see any justification

for expanding the concept in the field of standard securities or into non-corporate fields. Further, if such a remedy were introduced, it would presumably then either be necessary to immediately restrict its use where to do so would create an administrative receivership within the meaning of sec. 251 of the Insolvency Act 1986 (for example where the property that was the subject of a standard security was the only meaningful asset of a company), or risk creating a substantial loophole in the general insolvency regime (whereby a floating charge holder could not appoint an administrative receiver, but a standard security holder could). That does not appear to us to make sense.

45. Should any restriction be placed on the security holder's choice between the remedies of sale and management of the security property? If so, what form of restriction is appropriate?

(Paragraph 9.17)

**Comments on Proposal 45**

We consider this is ultimately a matter of policy on which we express no firm view. We would, however, make the following three observations. First, for completeness, our understanding would be that the *civiliter* principle discussed at para. 9.14 of the Discussion Paper has been interpreted as only engaged in a context where there is a likelihood that the security subjects would realise more than the secured debt: *Trustees of the 2004/2005 Eurocentral Hotel v.Hadrian Sarl* [2012] CSOH 59, para. [17] (Lord Hodge). In that context, we do not agree with academic criticisms of the principle as being contradictory. Secondly, that distinction seems to us to make sense. It maintains a consistency with, for example, general insolvency law where a debtor only has interest in challenging the actions of a trustee, liquidator, administrator etc. where there is a realistic prospect of any return: e.g. *Rica Gold Washing Company* (1879) 11 Ch. D. 36, pp. 42 – 43 and 45 (Jessel MR). We also note that such a threshold seems implicit in the Discussion Paper's framing of the potential harm to the debtor in para. 9.13, which refers to the potential of a debtor to access the value of the property in excess of the secured debt. Thirdly, for these reasons, we query what any statutory restriction would add to the *civiliter* principle. It would either just replicate it precisely, or it would risk conferring remedies on debtors who have no material interest in what is done with the secured property because it can never benefit them.

46. Do consultees agree that it should not be possible to vary the statutory provisions on exercise of remedies under a standard security?

(Paragraph 9.23)

**Comments on Proposal 46**

Yes, we agree for the reasons given in the Discussion Paper.

47. Do consultees agree that remedies under a standard security should continue to be exercisable by or on behalf of the security holder?

(Paragraph 9.24)

**Comments on Proposal 47**

Yes, we do not see any basis for suggesting that agents could not act on behalf of security holders.

48. What comments do consultees have as to the powers of postponed (or *pari passu*) security holders to exercise remedies without the consent of prior (or *pari passu*) security holders?

(Paragraph 9.28)

**Comments on Proposal 48**

In our view, the law is unclear. So any proposal for reform should seek to address the issue. We are not convinced by the middle ground of providing a remedy to prior and *pari passu* creditors of interdict where the exercise of any rights by the *pari passu* or postponed holders is "unreasonable". That is, in our view, too vague a criterion, and would serve to fundamentally dilute the stronger rights given by law to prior and *pari passu* creditors. If a requirement to obtain consent is considered too unwieldy (about which we are not able to offer a meaningful view as to whether that is true or not), we consider that could be addressed by administrative provisions designed to allow postponed holders to notify prior or *pari passu* security holders, and an opportunity to object to or veto any exercise of a particular remedy within a reasonable period of time.

49. (a) Should provision equivalent to section 27 of the 1970 Act on application of the proceeds of sale be made in any new legislation?

(b) Should this provision be extended to cover the proceeds of any remedy exercised under a security?

(Paragraph 9.31)

**Comments on Proposal 49**

In respect of (a), our view is yes (for the reasons given in the Discussion Paper).

In respect of (b), our view is, also, yes. We consider that this is probably implicit in the general law on ranking anyway, and should therefore be made express in any legislation so as to avoid any doubt about the issue.

50. Should new legislation on standard securities provide that a security holder may seek decree of ejection against any person in natural possession of the land or buildings in which the security is held where that person has no legal basis to occupy?

(Paragraph 10.11)

**Comments on Proposal 50**

We do not fully understand the proposal here. We make three comments.

First, we agree with the observations in para. 10.6 of the Discussion Paper on some of the linguistic difficulties in applying sec. 5 (1) of the 1894 Act because of its archaic terminology. This should be reformed along the lines proposed.

Secondly, however, in our view the essential purpose of sec. 5 (1) is to equiparate the owner of a secured property with an occupant without any right or title. This aligns them with the general common law on ejection. We do not, particularly, follow the difficulty that is perceived to exist in the relationship between the 1894 Act and the common law. We consider, in part, the Discussion Paper appears to proceed on the basis that the right of a security holder to seek decree of ejection is fundamentally split between the common law and the 1894 Act. This feeds into, for example, reliance being placed on *RBS v. Wilson* as vouching that proposition in para. 10.12. However, in our view, the 1894 Act simply recognises that the owner of secured property would otherwise be someone who previously had a good title to the property and against whom an action of removing would require to be taken. Sec. 5 is, therefore, a deeming provision designed to make it consistent with the common law on ejection. We are unclear from the proposal above whether this approach is intended to be retained, but we consider a deeming provision similar to sec. 5 is a sensible approach and should continue to be the case.

Thirdly, we are also unclear on the perceived difficulty with the reasoning in *Westfoot* mentioned in para. 10.8. The decision in *Westfoot* was that the Sheriff considered the reference to "personal occupation" in sec. 5, properly interpreted, applied to occupation by a legal or juridical person, and that there was no reason the remedy of ejection should not be available against such persons. We consider that the perceived difficulty perhaps flows from the approach in the Discussion Paper of suggesting there is some fundamental distinction between the remedy of ejection at common law and under sec. 5 of the 1894 Act. We consider that the reasoning in *Westfoot* should be followed and, therefore, reference to "natural possession" should not feature in any statutory formulation.

51. Do consultees agree that the only basis for ejection under a standard security should be the relevant statutory provision?

(Paragraph 10.13)

**Comments on Proposal 51**

No, see our previous answer.

52. When seeking to remove an assured or private residential tenant from the security property, should a security holder be required to obtain an order for possession under the relevant tenancy legislation?

(Paragraph 10.21)

**Comments on Proposal 52**

In our view, the Discussion Paper recognises this is an issue that has already been the subject of legislation as recently as 2016. If there is to be a change in that policy, we do not consider it is a matter for law reform.

53. (a) Should new legislation on standard securities provide guidance on how the security holder's duty of care in relation to moveables left in the security property may be discharged?

(b) If so, what guidance would be appropriate?

(Paragraph 10.26)

**Comments on Proposal 53**

The hallmark of any duty of care at common law is that it is relatively ill-defined and depends on the particular facts and circumstances of each case. If a common law duty of care is to be retained at all, we are unconvinced that any "guidance" would provide a large degree of comfort to security holders. The precise manner in which the Courts would weigh any such guidance in a particular case would remain uncertain. If there is a desire to provide certainty, the way to do that would be by way of a specific statutory scheme that governs the liability of a security holder for moveables and excludes any common law duty of care. If that were done, the legislation could specify how long moveables require to be retained, the precise notices that need to be served, provide for remedies to any debtor or third party whose possessions are disposed of or damaged in the event of failure to follow the statutory procedure, and otherwise provide for immunity from liability.

54. (a) In future legislation, should "taking possession" be defined to mean taking action to physically secure the land or buildings in which the security is held, including taking possession through a third party such as a tenant? If not, why not?

(b) Should the legislation include a non-exhaustive list of actions which meet the definition of possession? If so, which actions should be included?

(Paragraph 11.36)

**Comments on Proposal 54**

In our view, the answer to (a) is yes (for the reasons discussion in the Discussion Paper).

In our view, the answer to (b) is probably not. In particular, given that the legislation would effectively be enshrining the existing minimal approach to the concept of possession, it is difficult to see what a non-exhaustive list of actions would really add. It is difficult to conceive of particular actions being taken that would not involve as a constituent element either physical possession by changing the locks etc, or civil possession being exercised through a third party anyway. If there was some doubt about what is involved in a person "physically securing" a property then that might be capable of elaboration, but frankly we consider that phrase is pretty clear and unlikely to be difficult to apply in practice.

55. On entry into possession, should a security holder be able to exercise the rights of the owner or registered tenant in relation to the management and maintenance of the security property where:

(a) Management of the security property includes exercise of any rights required in connection with the aim of enforcing performance of the secured obligation;

(b) Maintenance of the security property includes any reconstruction, alteration or improvement reasonably required for the purpose of maintaining its market value?

(Paragraph 11.41)

**Comments on Proposal 55**

We agree with the comments in the Discussion Paper that: (a) an attempt to list the specific actions authorised by this power is neither necessary nor possible; and (b) that it might be useful if the broad principle set out by Gloag and Irvine was put on a statutory footing.

However, we find the wording of Proposal 55 a little difficult to follow. We consider the wording in any statutory provision ought to be clearer. For example, sec. 20 (5) (b) could just be reformulated along the lines: "the management and maintenance of the subjects (including any reconstruction, alterations, or improvements) reasonably required for the purpose of: (i) obtaining performance (or partial performance) of the secured obligation; or (ii) maintaining the market value of the subjects."

56. On entry into possession:

(a) Should a security holder assume the obligations of the owner or registered tenant in relation to the management and maintenance of the security property?

(b) Should this include responsibility for outstanding costs previously incurred by the owner or registered tenant in relation to the management and maintenance of the security property?

(Paragraph 11.46)

**Comments on Proposal 56**

In our view, the answer to (a) is yes, and the answer to (b) is no. We agree with the general principle that a security holder should assume liabilities for management and maintenance only upon taking entry into possession.

57. Do consultees agree that the security holder's right to collect rents and grant and administer leases under any new legislation should follow from entry into possession of the security property?

(Paragraph 12.3)

**Comments on Proposal 57**

Yes, for the reasons discussed in the Discussion Paper.

58. Should the security holder's remedy of collection of rents cover:

(a) Rents which fall due on or after the security holder's entitlement to rents arises?

(b) Rents which fell due prior to the security holder's entitlement arising, but have yet to be paid?

(Paragraph 12.7)

**Comments on Proposal 58**

In our view, the answer to (a) is yes. We see no reason to remove any such remedy from a security holder.

In our view, the answer to (b) is no. We agree with the observations in the Discussion Paper that it is inequitable that a security holder should be immune from liabilities or obligations that have accrued prior to entry into possession and also take the benefit of rights that have accrued. We, also, consider that if the debtor has an accrued right to payment from a third party tenant and the security holder is suitably anxious to ensure recovery of it then it has the same remedies of any creditor to obtain that asset, such as through arrestment or sequestration (at least where the secured obligation is payment of a sum of money).

59. In any new legislation, should the power to grant a lease be available under a standard security only where the security property is ownership of land or buildings?

(Paragraph 12.9)

**Comments on Proposal 59**

In our view, no. A standard security may be granted over any interest in land.

First, whilst this may not be the Commission's intention, the wording of this proposal would not include a lease (including, for example, a long lease) that itself allows subletting. We are unclear why the option of a security holder granting such leases or sub-leases would not be permitted.

Secondly, it could, at least conceptually, extend to other interests than just ownership or leases. It might include, for example, liferents or servitudes.

Thirdly, at least conceptually, land could be the subject of a burden that restricted the right to grant leases to certain people (for example in sheltered or retirement housing).

This all illustrates that it may be difficult to adopt such a bright-line rule as the one being proposed here. Whilst some of these examples are relatively rare, we consider the issue identified in the Discussion Paper could equally be addressed by making it clear that in exercising any power to grant a lease the security holder confers no better right than the debtor has under the particular interest in land.

60. In relation to the grant of (sub-)leases by the security holder:

(a) What comments do consultees have on the current use of this remedy in practice?

(b) What duration of lease should the security holder be entitled to grant without warrant of the court?

(c) Would the extension of the seven-year limit in relation to leases give rise to any debtor protection concerns? If so, what measures should be taken to address these concerns?

(d) What limits, if any, should be placed on the power of a security holder to grant a private residential tenancy?

(Paragraph 12.15)

**Comments on Proposal 60**

The issues focused in this proposal are not matters on which we consider we have sufficient experience to provide a useful comment.

61. We provisionally propose that, on entering into possession of the security property:

(a) A security holder should be entitled to exercise the rights of the owner or registered tenant relating to (sub-)leases or other rights of occupancy in respect of the security property; and

(b) A security holder should assume the obligations of the owner or registered tenant relating to (sub-)leases or other rights of occupancy in respect of the security property.

Do consultees agree?

(Paragraph 12.18)

**Comments on Proposal 61**

We agree. This overlaps with Proposals 55 and 56, and we refer to our comments on those.

62. Should a court order be required for the security holder to exercise the power of sale?

(Paragraph 13.28)

**Comments on Proposal 62**

We consider that court orders should continue to be required for security holders to exercise the power of sale in cases where the security property is used to any extent for residential purposes but not when the security property is used for other purposes.

63. Should the selling security holder continue to have the choice to sell by private bargain or by public auction? If not, what reform would you propose here?

(Paragraph 13.35)

**Comments on Proposal 63**

We agree that the selling security holder should continue to have the choice to sell by private bargain or by public auction. We would observe that some of the difficulties which arise in practice relative to the manner of sale do so because of a perception on the part of the debtor (and, arguably, the public at large) that sale by public auction is the less desirable of the two alternatives. The underlying reason for that preconception appears to be related to the duty to achieve the best price for the security property.

64. (a) Should the selling security holder be placed under a duty to take all reasonable steps to obtain (i) the best price reasonably obtainable, (ii) the market value of the security property or (iii) some other objective?

(b) Should the legislation include a non-exhaustive list of factors (capable of amendment by secondary legislation) to be considered by the court in determining whether this duty has been discharged? If so, which factors should be included, and why?

(Paragraph 13.39)

**Comments on Proposal 64**

(a) We consider that the selling security holder should continue to be placed under a duty to take all reasonable steps to obtain the best price reasonably obtainable. We agree with the observations in paragraph 13.37 that aligning the definition of best price to "market value" ignores circumstances where the best price which can be achieved is less than market value.

(b) We agree that the legislation should include a non exhaustive list of factors (capable of amendment by secondary legislation) to be considered by the court in determining whether the duty to obtain best price has been discharged by the security holder. We agree that the list of factors should include those mentioned at paragraph 13.38. We acknowledge that there will be other relevant factors as well but consider determination of those to be a matter of policy upon which others are better placed to comment.

65. Where a purchaser acquires property from the security holder exercising its power of sale under the security, should legislation provide that:

(a) The transfer is valid notwithstanding the lack of capacity of the debtor, the owner, or any other party entitled to receipt of notice of enforcement proceedings under the security; and

(b) The title acquired is protected against any challenge arising from extinction of the secured obligation or from defects in the process by which the security holder's power of sale is established, so long as certain conditions are fulfilled?

(Paragraph 13.47)

**Comments on Proposal 65**

We agree that legislation should provide protection to a purchaser acquiring property from a security holder exercising its power of sale under the security in relation to both (a) the validity of the transfer; and (b) any challenge to the title acquired by the purchaser, subject to conditions.

66. Do consultees agree that the conditions referred to in part (b) above should be as follows:

(a) The purchaser paid value for the security property;

(b) The purchaser was in good faith prior to the conclusion of missives, with the following factors taken into account in determining whether this requirement has been met:

(i) The purchaser's actual or constructive knowledge that the secured obligation had been extinguished;

(ii) The purchaser's actual or constructive knowledge of defects in the process by which the security holder's power of sale was established;

(iii) Attempts made by the purchaser to satisfy themselves that the purchaser has discharged its best price duty;

(iv) Whether the purchaser is a close associate of the security holder?

(Paragraph 13.47)

**Comments on Proposal 66**

We agree that (a) payment of value for the security property and (b) good faith prior to the conclusion of missives should be the conditions referred to at proposal 65(b). We agree that the factors noted at points (b)(i) – (iv) of proposal 66 should be taken into account when determining whether the good faith requirement has been met.

67. Do consultees agree that any new legislation should provide that:

(a) The security holder's remedy of sale of the security property includes the power to grant a disposition transferring ownership of that property.

(b) Registration of a disposition granted under this power has the effect of disburdening the property sold of the standard security, and of any *pari passu* and postponed securities.

(Paragraph 13.49)

**Comments on Proposal 67**

We agree that, in the interests of certainty, any new legislation should provide that

(a) the security holder's remedy of sale of the security property includes the power to grant a disposition transferring ownership of that property; and

(b) registration of a disposition granted under this power has the effect of disburdening the property sold of the standard security, and of any *pari passu* and postponed securities.

68. Is any reform required to the foreclosure process? If so, which reforms would be appropriate?

(Paragraph 14.22)

**Comments on Proposal 68**

We agree that foreclosure is rarely sought in Scotland.

We also agree that a restatement of the law in new legislation and modernisation of certain aspects would be beneficial.

For the reasons set out in paragraph 14.19, we consider that the requirement for a court order for foreclosure should be retained.

Considering the public perception of sale by public auction in situations where security holders are exercising their remedies (as noted in our comments under proposal 63), we agree that the requirement for attempted sale by private bargain should be introduced. However, we do not consider that sale by private bargain necessarily has to replace sale by public auction.

We do not consider that there is a need to limit the court's discretion in relation to disposing of an application for decree of foreclosure. We consider that the rarity of foreclosure proceedings is a factor weighing in favour of retaining judicial discretion.

69. (a) Should the debtor be liable to the security holder for expenses reasonably incurred in exercising the security?

(b) Should the expenses of litigation be "reasonably incurred" only to the extent of any award by the court or agreement between the parties?

(c) Is there an alternative approach to the debtor's liability for expenses that you would consider more appropriate, and if so, why?

(Paragraph 15.13)

**Comments on Proposal 69**

(a) We agree that the debtor should be liable to the security holder for expenses reasonably incurred.

(b) To provide clarity, we agree that the expenses of litigation should be "reasonably incurred" only to the extent of any award by the court or agreement between the parties.

(c) We consider this to be a matter of policy, upon which we have no comment.

**General Comments**

We have nothing further to add to the above comments.

Thank you for taking the time to respond to this Discussion Paper. Your comments are appreciated and will be taken into consideration when preparing a report containing our final recommendations.