

**Scottish Law Commission – Discussion Paper on Heritable Securities: Default and Post-Default
(DP No. 173)**

Response (March 2022)

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General

We welcome the opportunity to respond to the Discussion Paper (“DP”). We agree with the SLC’s intention to reform the law in this area and support its proposals, subject to the points made below. The DP provides helpful coverage of the existing law and offers welcome clarity in its analysis of issues. We also acknowledge the careful use of terminology in the DP.

In addition, we look forward to the third Discussion Paper and understand the justification for its focus on sub-security arrangements and security in respect of non-monetary obligations.

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)

While we do not have specific information or data in relation to this, the proposals to improve, clarify and simplify the law should, logically, have a positive economic impact.

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)

We can see some justification for expressly including such a duty, particularly given the powers that a standard security holder has and the potential impact of exercising a standard security on the debtor or security property owner or others. In addition, a standard security holder should not expect to be allowed to act unreasonably and such a duty ought to provide greater uniformity of behaviour among creditors. An equivalent duty was also recommended in relation to moveable transactions. However, there are questions regarding how reasonableness in this context will be determined or ascertained and there will be uncertainty for standard security holders as to what precisely is required to comply with the duty, particularly in the early stages of its existence. As suggested in the DP, “unscrupulous debtors” could use the duty “to raise highly speculative or even unfounded challenges to the exercise of the security”, which could ultimately impact negatively upon the provision of finance. Perhaps the duty would have wider appeal if it could be narrowed or limited somewhat; however, we appreciate this would be difficult to do. Including examples of relevant conduct that falls or does not fall within the duty in the Report and/or the Notes on the Draft Bill might assist but will be troublesome to achieve and will not completely resolve the issue.

Of course, even though the standard security is a statutory form of security, the common law is still considered to apply to it in a number of ways. It could be contended that the various duties applicable to a

secured creditor under the legislation and at common law collectively amount to something approximating the proposed express duty, and there is probably scope for the courts to develop the law further in that direction. Perhaps that would be a more amenable approach for a wider range of parties. These points could even be made in the Report, to act as a marker for the courts and other parties in future.

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

(Paragraph 2.38)

The approach seems sensible, subject to the caveat in paragraph 2.37 and the points made in our response to the previous Discussion Paper (question 54).

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)

Given the resource implications and the very small number of such securities still in existence, the law regarding enforcement of such securities should be left alone (i.e. to “wither on the vine”).

As an aside, we would be curious to know whether the SLC is aware of any enforcement activities involving *ex facie* absolute dispositions in recent times. It would, of course, also be interesting to know how many *ex facie* absolute dispositions continue to exist but we understand that is almost certainly not ascertainable.

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

(Paragraph 3.24)

While there might be a risk regarding the alteration of the meaning or application of the principle if it is restated in legislation, it is already included in various ways implicitly (including in the 1970 Act) and in the Titles to Land Consolidation (Scotland) Act 1868, s 120, and it would be helpful from an accessibility point of view if there was a clear statement of the principle in legislation. Hypothetically, if a new security were to be introduced now, it would be advisable to specify a clear ranking rule or principle. As a result, it seems sensible that new legislation on the standard security, as a statutory form of security (even though not new), should include the basic ranking position. This is particularly true given that other provisions of the legislation, including s 13 and s 27, refer to ranking in various ways. There could be a straightforward statement that a standard security ranks from when it is registered (i.e. when its holder obtains a real right) against other standard securities and other types of security, subject to any other enactment or rule of law that provides otherwise (which can encompass ranking agreements and rules relating to floating charges etc).

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)

We can see some merit in not allowing a subsequent standard security holder to restrict the priority of an earlier standard security by giving notice. The subsequent security holder is voluntarily entering into the secured transaction and practice generally will require for the first-ranking security holder to either give permission or to rank first for the whole amount due. However, we do wonder whether there is a stronger argument in favour of continuing to allow involuntary security holders (e.g. diligence creditors and parties with charging orders) to restrict the standard security holder's priority, even though in practice the standard security holder will be unlikely to extend further sums to the debtor if the security property becomes subject to involuntary security. On the other hand, it could be contended that at least some parties who acquire involuntary security took a risk in entering into an unsecured credit agreement with the creditor and it would be unfair to restrict a standard security holder but not one of these involuntary security holders. Yet there are other involuntary security holders who seem to deserve such protection, and it may not be feasible to distinguish between different types of involuntary security holder. At common law, notice of diligence would have a restrictive effect and this is also true for e.g. assignation in security (see e.g. MacPherson, *The Floating Charge*, para 9-24 and the sources cited there). In any event, we think that this issue needs further consideration.

One additional technical point is that if the provisions in s 13 are to be removed, changes would also seemingly need to be made to the proposed s 13A, which would be inserted by the Bankruptcy and Diligence etc (Scotland) Act 2007, s 85 (if it is brought into force). This relates to the effect of a subsequent land attachment on the ranking of a standard security and refers to s 13(1).

If restriction of priority is to be possible (at least in some instances), we consider that the post-notice advances by the prior security holder should simply have lower priority than those of the other security holder, rather than being unsecured.

7. Do consultees agree that under any new legislation:

(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)

Yes, the parties should be free to enter into a ranking agreement intended to vary the terms of the security. It should be possible to do this not only with standard securities but between a standard security and other forms of security over the property as well (i.e. involuntary securities), albeit that this would be unusual. Such agreements should be set out in writing and registration should be required to vary the terms of the standard securities concerned.

One further point is that perhaps some attention can be given to the interplay and operation of parallel regimes regarding ranking agreements e.g. involving a standard security and a floating charge.

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)

Yes, this seems a sensible and straightforward approach and avoids difficulties that exist in the present law.

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)

We consider that there might be some merit in continuing to provide that certain insolvency events would allow the security holder to exercise remedies. We appreciate that this would almost inevitably be provided for by agreement if not specified in statute, but we nevertheless think that it might be useful to have these as default circumstances in which remedies might be exercised, in the same way as a floating charge will specify the circumstances justifying the appointment of a receiver but the legislation also provides for certain circumstances which will justify this irrespective of the terms of the security (Insolvency Act 1986, s 52). In order to keep matters simple, however, we would not make these provisions variable by the parties. If this approach is adopted, we consider that the events to be specified could usefully be reviewed. For example, the outdated reference to notour bankruptcy in the current legislation should be changed to apparent insolvency; consideration might be given to including specific reference to an award of sequestration (although we appreciate that such an award itself constitutes the debtor's apparent insolvency and so would be caught by that provision); and consideration might be given to whether, in the case of a company, entering administration or other arrangements such as a restructuring plan under Part 26A of the Companies Act 2006 (which requires the company to be, or be likely to be, in financial difficulties) should be included. (We appreciate that in the case of administration, the statutory moratorium would prevent the exercise of remedies without the consent of the administrator or the court, but that is a separate issue.)

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)

We agree with the proposal and consider that having one form of notice is preferable to the current situation.

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

(Paragraph 5.15)

We agree with this as it will provide certainty and consistency.

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)

From an accessibility point of view, we can see the merit of including the form of the default notice in primary legislation. However, there is also value in the flexibility provided by secondary legislation. We realise they are controversial, but perhaps “Henry VIII provisions” can be used whereby primary legislation gives powers to amend such legislation by subordinate legislation.

In terms of (b), we agree with the suggested list of key information to be included in the default notice. As regards (c), perhaps the information should also include reference to the relevant legislation (including particular provisions) under which the default has occurred and the standard security may be exercised.

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

(Paragraph 5.20)

Yes, we agree.

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)

We broadly agree with the proposals. However, attention should be given to whether service should also be made on a liquidator or administrator or equivalent in corporate insolvencies, given the requirement noted for personal insolvency, albeit that we appreciate there are certain differences between the position of a trustee in sequestration and a liquidator or administrator or equivalent. Consideration should also be given as to whether there should be service on a trustee under a protected trust deed and on a judicial factor under s 11A of the Judicial Factors (Scotland) Act 1889.

Regarding 14(b), we note that it may be helpful to give further thought to what happens where there are delays in obtaining confirmation of executors.

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 incapax, should service be made solely on the guardian or attorney on that adult's behalf?

(Paragraph 5.31)

While we understand there may be some issues regarding serving notice on incapax parties, there is also an argument that the benefit of serving notice on both the incapax party and the guardian outweighs the benefit of serving notice only on the guardian, at least in some instances. As regards the reference in paragraph 5.30 that an incapax party is by definition vulnerable and that service on them is inappropriate, it would be helpful to clarify what is meant by "inappropriate" here and whether this would be applicable in every situation involving an incapax party. Even if every incapax party is vulnerable, it does not necessarily follow that they should not be served with a default notice and there may be instances where such a party may wish to (or ought to) receive the default notice.

We also note that generally there needs to be clarity regarding how a security holder becomes aware of a guardian acting for the intended recipient of a default notice. In addition, we consider that written confirmation to the security holder should be required.

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)

Yes, we agree.

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

(Paragraph 5.41)

We cannot think of any other appropriate method of service.

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)

Yes, we agree, especially given that it is consistent with the recommendation for moveable transactions.

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)

We think there may be some merit in giving parties the opportunity to agree in advance on a varied length of notice to suit various circumstances provided that a minimum length is prescribed. We also note that having different timescales may be preferable for the parties in some instances, in order to take account of different types of defaults that may occur and the likely timescales necessary to rectify those defaults.

In terms of a (minimum) time limit for compliance, we consider two months may be too long a period (generally speaking) and 14 days is rather short but is used for some other timescales in this area of law, including the period for expiry of a charge for payment. 21 days is also probably too short, but is used in other areas of the law of security rights, e.g. registration of company charges, and of insolvency, e.g. in the context of statutory demands for payment of debt. Our preference would probably be for a minimum period of one month, as this gives a fairly significant amount of time and strikes a good balance, and has some basis in the current law (i.e. the period to comply with a default notice). 28 days or 40 days would also be appropriate alternatives to one month.

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);

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

(Paragraph 5.48)

Yes, provided that (c) is read as “pari passu or postponed security holders” (and not “prior or pari passu securities”), as per paragraph 5.47 of the DP and s 19(10) of the 1970 Act.

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)

No, it should not be excluded from application to any new standard securities legislation. We consider that it may be helpful to cross-reference s 21 of the 2010 Act in the new legislation or that an explanatory note to the legislation should do so, given the apparent intention that there will not be a specific provision in the new legislation. We think that having one applicable provision and test is better than having two sets of provisions or tests, even if those provisions/tests are closely aligned with one another.

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)

Yes, we agree with this proposal, not least because it will be less complex and costly than what is involved in Court of Session petition procedure.

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)

We consider that a five-year period should continue to apply for reasons of continuity and consistency.

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)

If a default has been remedied then it stands to reason that a default notice corresponding to that default should expire and it should not provide a valid basis for the exercise of remedies going forward. However, the costs incurred by the creditor up to the point of purging of the default should be borne by the debtor.

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)

Yes, 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)

Yes, subject to the point regarding reasonable expenses in para 6.21 of the DP.

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)

Yes.

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)

Yes, for reasons of continuity and consistency, and there also seems to be no compelling reason to change the current position.

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)

Yes.

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)

If the policy intention here is focused on a natural person losing their home, then we consider that it would be reasonable to disapply all of the enhanced protection measures where the sole owner or, in the case of joint owners, all owners, of the security property are juristic persons. However, if instead or in addition, there is an intention to protect a debtor qua debtor, then we can see that there might be some merit in a more selective disapplication of the measures.

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)

No, we consider that none of the enhanced protection measures should be disapplied where the sole or any joint owner of the security property is a natural person.

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)

While we can see that the proposed property criterion has advantages in terms of certainty and ease of application, we are concerned that, as noted in para 7.59, it will allow cases to be brought within the ambit of the enhanced protection measures which arguably should not be within them, with the result that the provisions do not align fully with the policy intent behind the legislation. While recognising that it may give rise to some practical difficulties, we would therefore prefer a formula based on occupation. We are, however, content with the use of the term “dwellinghouse” and agree that irrespective of whether or not they are linked to occupation of it, the enhanced protection measures should apply where the security property is or includes a dwellinghouse.

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)

Yes, this would aid clarity and accessibility.

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

Yes.

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

We suggest that if the proposed property criterion is used as opposed to any criterion taking into account occupation, consideration should be given to providing for other exceptions for properties which are in practice not sole or main residences, such as second homes, properties used for holiday lets/Airbnb or otherwise as investments rather than homes as such. Consideration could also be given to excluding properties which are empty (for example because the owner has moved but the property has not yet been sold).

(Paragraph 7.62)

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 the property and to the local authority in which the property is located.

Do consultees agree?

(Paragraph 7.67)

Yes.

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

(Paragraph 8.6)

We do not have any suggestions to make here, except that it could be useful to include a requirement that the debtor should be informed of the particular steps that may be taken if there is no resolution and, potentially, other consequences that may arise in these circumstances. This information would likely help the debtor in their decision-making. A similar requirement exists in the FCA Handbook for debtors previously in arrears within the past 12 months – MCOB 13.4.4. The FCA's approach could be adopted (i.e., limiting the requirement to debtors formerly in arrears), or the requirement could apply generally.

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)

Yes, this seems sensible.

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)

Not being in practice, we are not aware of any other difficulties.

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)?

Yes. This approach works in other contexts, such as the family home in sequestration/protected trust deeds, and there seems to be no reason to adopt a different approach here.

(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?

Yes, this seems reasonable.

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

We do not have any suggestions to make here.

(Paragraph 8.14)

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)

No. The courts regularly carry out such balancing exercises without further statutory guidance, including in the context of dealing with the family home in sequestration/protected trust deeds, and we consider that

they are capable of carrying out the necessary balancing exercise in this context without further statutory guidance.

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)

No, we do not see the need for any such changes.

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?

Yes.

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

No. We can foresee that there might be cases, for example, where the owner is happy to remain in the property while it is marketed and move when it is sold, so it does not seem logical that the property must be confirmed to be unoccupied. The issue of occupation may be relevant if the creditor's intention is to let the property rather than sell it, but that is a separate issue.

(Paragraph 8.22)

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)

Yes, the new legislation on standard securities should make available the same remedies under the current legislation. We note the generally accepted position regarding standard securities and malls and duties specified at para 9.3 but see Prof Gretton's discussion at para 396 of "Diligence" in SME, vol 8, which indicates there may be some dispute regarding the extent to which this is the case. Given the statement in para 9.3 and the fact that the Bankruptcy and Diligence etc (Scotland) Act 2007, s 207(1), would abolish malls and duties if brought into force, it is probably not worthwhile to do anything further on this but we mention it for interest and potential consideration.

We have not been able to identify any remedy not currently provided for, except perhaps the ability to grant rights to use the property short of a lease and corresponding rights to receive payments for such use.

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)

Making receivership available as a remedy would be a rather complicated change and it does not seem to be necessary or justified. English law has a long history of using receivers to enforce security but that is not true here. The story of receivership and floating charges in Scots law also provides a cautionary tale.

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)

As the common law may already place restrictions on a security holder, we can see some merit in not having statutory restrictions. However, given the uncertainty regarding the common law position, and the possibility for it to be departed from in future, it may be sensible to make statutory provision if the debtor and/or others could be prejudiced by the security holder having a free choice of remedies. This could be done by providing that sale is the primary remedy and another remedy will only be used if sale is not possible or it can be shown that it is not reasonable in the circumstances. Another approach would be to make freedom to choose remedies the default position, but the debtor and other relevant parties can apply to restrict the security holder's freedom if a particular remedy or remedies would cause unjustified prejudice. On balance, we would prefer this approach and it should be noted that the choice of a management remedy rather than sale could actually benefit the debtor if it results in repayment and return of the property to the debtor. There is probably a stronger need for a statutory provision here if there is to be no statutory duty to conform with reasonable standards of commercial practice.

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)

We agree.

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)

We agree.

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)

The "middle ground" approach, whereby prior and *pari passu* holders have a right to seek interdict against a *pari passu* or postponed holder who seeks to exercise remedies where it would be unreasonable to do so, seems reasonable to us. Any approach adopted should seek to avoid the possibility of multiple different attempts to enforce by different parties, which would be confusing and a waste of resources.

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)

Yes, we think that provision equivalent to s 27 of the 1970 Act on application of proceeds should be made in any new legislation. This provision should be extended to cover the proceeds of any remedy exercised under a security.

There are some difficulties in relation to s 27 where a floating charge is involved (see the discussion at MacPherson, *The Floating Charge* (2020), para 6-09 ff). We appreciate that floating charges are beyond the scope of this project; however, if a new provision equivalent to s 27 is to be introduced, it could specify that where a security in the distribution order is an attached floating charge, payment (for all remaining proceeds available) should be made to the liquidator, administrator, or receiver, as appropriate, and not to the floating charge holder directly. If this change is not to be made, then it would at least be useful for the Report for this project to confirm the foregoing is the appropriate approach for any new provision equivalent to s 27, if there is an attached floating charge and a standard security holder is exercising a remedy.

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)

We agree with this, for the reasons given in the DP.

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

(Paragraph 10.13)

We agree with this for clarity and to avoid potential confusion.

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)

Yes, for the reasons given in the DP. One point to consider is that where a tenancy has been granted without obtaining the security holder's consent, this may be something that should be taken into account in the process for obtaining an order for possession. If this was considered desirable, it would require amendment of the relevant legislation.

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?

Yes, new legislation on standard securities should 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?

Appropriate guidance should include details about how long moveables should be retained for, what steps have to be taken to contact the owner or otherwise bring the matter to their attention, and how the moveables should be dealt with after any relevant time period has expired (e.g. whether the security holder can simply dispose of the items or whether, perhaps, certain items should be sent to a last known address of the former owner of the security property).

(Paragraph 10.26)

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?

Yes, the term should be defined widely in this way, as suggested in the DP.

(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)

We can see some merit in including a non-exhaustive list of actions that may meet the definition of possession. This will enhance understanding of the intended scope of the definition and simplify the application of the law. We consider the following actions by the security holder or their agent relevant:

- i. ejection of the occupants of the security property;
- ii. changing the locks to the security property;
- iii. entering into civil possession and thereby exerting control through a third party, such as a tenant, which may include giving tenants notice to pay rents to the security holder or their appointed nominee or otherwise exerting rights in relation to tenants;
- iv. securing the boundaries of the security property (e.g. by placing boundary markers), particularly where the property is an undeveloped plot of land or a large property;
- v. engaging management or security services or comparable agents for the security property;
- vi. other acts that show that the security holder has taken over the management and/or control of the security property. (This could include e.g. removing signage and/or other indicators relating to the previous occupant(s).)

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)

Yes to both.

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?

Yes, we agree subject to our response to question 56(b) below.

(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)

We think that, as a general rule, security holders should not be liable for such outstanding costs. We consider that, conceptually, debts previously owed by the owner or registered tenant in relation to the management and maintenance of the security property are personal obligations and therefore do not transmit to a security holder. This is in line with the decision in *David Watson Property Management*. There may be other reasons why it is better not to transfer such outstanding costs to the security holder. For example, it may make the security holder instantly exposed to significant debts upon taking possession and consequently at risk of court action for debt recovery. That seems contrary to the purpose of exercising the security, which is to ensure the payment of the security holder's debts.

However, we can see the policy justification for attributing outstanding costs arising from shared repairs to the security holder as discussed in the DP. It will allow for more straightforward and timely resolution of issues involving multiple properties. Thus, as an exception to the general rule, we would tentatively support the security holder assuming the outstanding costs arising from shared repairs; however, such costs should be recoverable from the debtor and covered by the security.

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)

Yes, we agree.

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?

Yes.

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

(Paragraph 12.7)

We consider that rent arrears that fell due prior to the security holder's entitlement arising should be recoverable by the security holder. We broadly agree with the arguments advanced by Halliday, and Cusine and Rennie, as discussed in the DP, and note that s 20(5)(a) of the 1970 Act, which assigns to the security holder "all rights" of the owner relating to leases, could be seen to have the effect of transferring rights to receive rent arrears. Unlike debt obligations, rents are conceptually assignable. We also consider that granting the security holder the right to recover rent arrears fulfils the primary purpose of a security, which is to use the proceeds arising from the security property to satisfy the creditor's debts where the debtor defaults. From this perspective, it seems practical to give the creditor priority, as the law could assume that the debtor would have used the rent to settle the debt had the rent been paid as and when due.

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

(Paragraph 12.9)

Yes.

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?

We have no recent practical experience on this point and so are not in a position to comment in detail. However, we agree that the seven-year limit is unduly restrictive in some instances and makes the remedy less attractive than it might otherwise be.

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

We think a longer duration of lease should be available for commercial properties. We can see some merit in a period of 15 years; however, a longer or shorter period could also be justified.

(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?

Yes – one concern is that a longer lease would deprive the debtor of the use of the property for an extended period of time. Also, there may be instances where the debtor considers the sale of the security property a better way of extracting value from the security property. Allowing the secured creditor to grant a longer lease without a court warrant could deny the debtor (and other creditors) the ability to extract such value and access surplus proceeds that would have been derived from the sale.

We consider that these concerns can be addressed by, as suggested in the DP, giving the debtor a right to challenge the grant of the lease where it is unreasonable in all the circumstances of the case.

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

We consider that seeking the permission of the court in order to grant a private residential tenancy (“PRT”) may be justified, given that such tenancies are not of fixed duration. A court should obviously be cognisant of the fact that the PRT can ultimately be brought to an end in certain ways, with eviction obtainable on the basis of various specified grounds (specified in the 2016 Act, Sch 3). To avoid multiplicity of court applications, the court’s permission for granting a PRT could be requested when a warrant is sought due to the enhanced debtor protection measures.

(Paragraph 12.15)

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)

Yes to both.

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

(Paragraph 13.28)

No, except where the enhanced debtor protection measures or other exceptions apply.

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)

Yes, the selling security holder should continue to have the choice to sell by private bargain or by public auction.

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?

The selling security holder should be placed under a duty to take all reasonable steps to obtain the best price reasonably obtainable – i.e. the duty imposed by section 25 of the 1970 Act should be retained. There does not seem to be any real need or demand for change on this point.

(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)

Yes, a non-exhaustive list of particularly important factors could be included. Those factors could include the steps that were taken to advertise the property and whether more could have been practicably done on that front; the length of time during which the property was exposed for sale; the state of the market in which the property was being sold at the time of sale and evidence that some other purchaser would have been prepared to pay more for the property; whether or not professional advisers, such as marketing agents, have been consulted/employed (and how they were chosen and instructed may also be relevant); the nature and extent of advertising and how the property could practicably be advertised; and, where the seller has a choice of offers from different potential purchasers, the reasonableness of the seller's choice.

It might also be worth stating that certain circumstances will not, without more, be significant. For example, it could be stated that the mere fact that more emphasis could have been placed on the land's development potential when the land was advertised does not, without more, constitute a breach of duty. Alternatively, however, it might be worth leaving such specific points to cases like *Dick v Clydesdale Bank Plc*, which, assuming the "price" duty from the 1970 Act, s 25 is replicated in substantially the same terms in any new legislation (as suggested above), could still afford helpful guidance.

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)

Yes to both.

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)

Yes.

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)

Yes to both.

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

(Paragraph 14.22)

The retention of the need for a decree for foreclosure to be obtained, combined with abolition of the requirement for the attempted sale of the property to be by public auction, seems sensible for the reasons given in the DP. There should be judicial oversight of foreclosure for the debtor's protection, but requiring a public auction duplicates the oversight provided by a decree and may not lead to the best price. The proposal that the court's discretion be constrained also seems sensible.

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)

The debtor should be liable to the security holder for expenses reasonably incurred in exercising the security. It is agreed that a reasonableness test, as opposed to a rigid set of conditions, would afford an appropriate degree of flexibility. That said, inclusion of a non-exhaustive list of factors concerning reasonableness would not necessarily detract from that flexibility.

The proposal to limit the expenses of litigation which are reasonably incurred to the extent of a court award or agreement between the parties seems sensible for the reasons given in the DP.