



Scottish Law Commission

promoting law reform

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DISCUSSION PAPER ON HERITABLE SECURITIES: NON-MONETARY SECURITIES AND SUB-SECURITIES

The Scottish Law Commission today publishes a third Discussion Paper consulting on reform of the law of securities granted over land and buildings in Scotland.

Heritable securities (often referred to as mortgages) are at the heart of many high-value commercial property and finance transactions. This paper explores two complex issues arising in this area of law, namely heritable securities in respect of non-monetary obligations and sub-security arrangements.

The term “non-monetary obligation” generally refers to an obligation to do something other than pay a debt. Granting a heritable security in respect of an obligation of this type is a common occurrence in particular types of property transaction, for example an obligation of a land owner to sell their land under an option agreement. Confusion arises as to how a heritable security in respect of a non-monetary obligation operates to enforce performance of that obligation when, in reality, the security can only be used as a means of extracting money from the secured asset.

A sub-security arrangement, in this context, describes the situation where a heritable security is taken over an existing heritable security. Unlike a more conventional security, where the security property will often be land, the security property in this arrangement is itself a security. The creation of such sub-securities is viewed as an important step in high-value securitisation and debt warehousing transactions in the commercial finance sector. While the current law permits the creation of these “secondary” or “piggyback” standard securities, questions arise over the conceptual soundness and practical utility of this approach.

This Discussion Paper looks at the use of heritable securities in both of these contexts, and seeks views on provisional proposals for reform to deal with the difficulties arising under the current law.

The Discussion Paper considers in detail:

- the historical background to the law relating to non-monetary securities together with their use today;
- proposals for reform in relation to non-monetary securities to reflect the fact that they can, in reality, only be used to generate money for the security holder in the event of default;
- a new scheme for protecting contractual obligations to transfer land – referred to in the paper as the conditional advance notice scheme;
- the law relating to heritable sub-securities and their use in a typical securitisation arrangement;
- a proposal to make it incompetent in future to take a standard security over a standard security; and
- the law in relation to assignments in security of heritable securities.

We seek views from consultees on 19 questions, including:

- Whether a standard security should (i) no longer be capable of securing a non-monetary obligation, but may secure substitutionary monetary claims, or (ii) be capable of securing a non-monetary obligation, but with the security holder only entitled to damages on default?
- Whether the law should provide a means by which contractual obligations to transfer land can be protected beyond the usual contractual remedies?
- Whether the grant of a standard security over a standard security should cease to be competent?
- Whether it should be possible to assign in security a standard security?

While the general ethos of the project is to aim for “evolution, not revolution” in the law, our provisional proposals are designed to achieve substantial improvements across these two technically challenging areas.

The Commission is very keen to hear from everyone with an interest in the issues raised in the Discussion Paper. Comments can be made until 29 September 2023, and will help shape the recommendations to be made in our final Report.

Professor Frankie McCarthy, the lead Commissioner, said:

“This is the third and final Discussion Paper for the heritable securities project. It considers two issues in the law of heritable securities which are important in complex, high value commercial property and finance transactions: non-monetary securities and sub-securities. The Discussion Paper necessarily covers a lot of technical legal detail. It puts forward proposals to resolve ambiguities in the current law which might be seen to hamper the kind of transactions under consideration taking place in Scotland. Importantly, the paper proposes a new scheme to protect contractual obligations to transfer land. This is something that has been called for by practitioners from the outset of the project. I look forward to hearing from consultees on the questions set out in the paper.”

FURTHER INFORMATION SECTION

1. The Scottish Law Commission was set up in 1965 to promote the reform of the law of Scotland. The Chair is the Rt Hon Lady Paton, a Court of Session judge. The other Commissioners are David Bartos, Professor Gillian Black, and Professor Frankie McCarthy. The Interim Chief Executive is Charles Garland.

2. Further information can be obtained by contacting Stephen Crilly, Scottish Law Commission, Parliament House, 11 Parliament Square, Edinburgh EH1 1RQ (Tel: 0131 244 6605; email info@scotlawcom.gov.uk).

3. The paper will be available on our website at <https://www.scotlawcom.gov.uk> as early as possible on 29 June 2023.