

## KEY POINTS

- Current Scottish moveable transactions law is undoubtedly unfit for the needs of twenty-first century commerce.
- The Scottish Law Commission's recent Report on Moveable Transactions proposes incremental reform, as there was little enthusiasm for a UCC-9/PPSA-type scheme at present in Scotland.
- Key proposals include registration of assignments (assignments) in a new electronic Register of Assignations and a new registered "fixed" security called a statutory pledge to be introduced in respect of corporeal (tangible) moveable property, intellectual property and financial instruments.

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# Moveable transactions law reform coming in Scotland?

In this article, the authors outline the proposed new regimes set out in the Scottish Law Commission's Report on Moveable Transactions and illustrate some of the opportunities that would become available as a result of the new regimes' flexibility.

On 19 December 2017, Scotland's law reform body, the Scottish Law Commission (SLC), published its much-anticipated Report on Moveable Transactions (<https://www.scotlawcom.gov.uk/news/improving-access-to-finance-in-scotland/>). The Report, which is in three volumes and includes a 124-section draft Bill, makes more than 200 recommendations. These relate broadly to what common-law jurisdictions call "personal property security law". It is hoped that the Scottish government will move forward swiftly to implement the SLC's Report in order to provide Scotland with a coherent modern moveable transactions law, in particular in relation to: (i) outright and security assignments of claims; and (ii) fixed security rights over corporeal moveables, intellectual property and financial instruments.

The Report recommends reform of three main areas of moveable transactions law: (i) assignment of claims; (ii) security over corporeal moveable property; and (iii) security over incorporeal moveable property.

Area (i) involves the assignment (assignment) of claims. By "claim" is meant a right to the performance of an obligation. This is usually the right to be paid money, eg under an invoice, but may be a right to performance of a non-monetary obligation. "Claims" include monetary (but not non-monetary) claims in relation to land. Area (ii) involves security over corporeal (tangible) moveable assets, such as vehicles and equipment. Area (iii) involves security over incorporeal (intangible) moveable assets and in particular financial instruments and intellectual property.

As will be seen below, Scottish law in these fields is not currently fit for modern purposes. Its inadequate and cumbersome nature creates

inefficiencies and impediments for Scottish businesses and others dealing with Scottish moveable assets.

The SLC has accordingly recommended new regimes under which assignments of claims and a new form of "statutory pledge" over corporeal moveables, intellectual property and financial instruments will take effect when: (i) an assignment/pledge document is registered in a new electronic Register of Assignations or Register of Statutory Pledges; (ii) the assignor/provider of the pledge has become owner of an asset assigned/pledged under the document; (iii) the assigned/pledged asset has become identifiable; (iv) for assignment, any condition precedent to the assignment referred to in the document has been satisfied.

The SLC recommends that elements of the current regimes are preserved. For example, a modernised form of the present notice (intimation) to counterparties could continue to be used in place of registering an assignment document. Similarly, delivery of the asset may continue to be used to take a traditional pledge over corporeal moveables rather than registration. Transfers of intellectual property or of financial instruments may also continue to be taken for security purposes. Additionally, possession and control as envisaged in the Financial Collateral Arrangements (No 2) Regulations 2003 may be used to effect an assignment or pledge of financial collateral under the proposed new regimes, in place of registration.

Some may regard the proposed reforms as unambitious, as they do not follow the notice filing or functional approaches of personal property security legislation in other jurisdictions. But, as discussed in more detail

below, the recommendations reflect instead a pragmatic, incremental response to practical problems which builds coherently on Scottish legal structures in the context of a unified UK market. They may also provide a base for more radical reform in the future.

## WHAT IS WRONG WITH THE CURRENT REGIMES?

The SLC's Report and preceding Discussion Paper (both available via the link above) describe at length what is wrong with current Scottish regimes for assignment and security over moveable property. These have been regarded as in need of reform for a long time. For example, W M Gloag and J M Irvine, *Law of Rights in Security* (1897), pp 187-188 suggested that a system based on the English bills of sale legislation might be introduced. But this has never happened, even as bills of sale now are set to be replaced by goods mortgages following recommendations of the Law Commission for England and Wales. The only significant development in the last hundred years has been the introduction of the floating charge in 1961. But the limitations of this type of security, for example the fact that only certain incorporated debtors can grant it and that it has a restricted ranking in insolvency, are well known. It is worth highlighting some particular problems with the current regimes:

- **All regimes:**
  - doubt on transfer of/security over assets not existing and owned at time transferred/secured;
  - doubt on required levels of identification of bulk assets transferred/secured;
  - conceptual/practical problems creating multiple levels of security by title transfer;
  - uncertainty on practical documentation requirements.
- **Assignment:**
  - no effect unless and until intimated to counterparty;
  - intimation under the Transmission of

## Feature

Moveable Property (Scotland) Act 1862 – doubt on equivalents, electronic methods and acknowledgement;

- doubts on effects of assignment subject to a condition;
- doubts whether continued payment to assignor invalidates assignment.
- **Pledge of corporeal moveables:**
  - requirement for delivery prevents use by debtor of assets pledged;
  - uncertainties as to permissible types of delivery and enforcement.
- **Security transfer of intellectual property:**
  - need for operating licence back to transferor;
  - complexity of infringement enforcement;
  - assignment problems for intellectual property licences.
- **Security transfer of financial instruments:**
  - assignment problems for contractual financial instruments;
  - security transferee requires to become registered holder of registered securities;
  - need for voting proxies/dividend mandates back to transferor;
  - real/perceived risks to subsidiary status;
  - real/perceived risks under people with significant control regime.

Many of these problems do not exist in English law because of the availability of equitable assignments and fixed charges. The proposed new assignment and pledge regimes described below would substantially address these problems arising from the inadequacy of the current law in Scotland.

### THE APPROACH TAKEN TO REFORM

There have been a number of unsuccessful earlier attempts to reform moveable transactions laws on a UK-wide basis (eg the Diamond Report of 1989) and Scotland-only basis (eg the Murray Report of 1994). The SLC has sought to learn from this. It is generally agreed in Scotland that some of these attempts took too radical an approach by proposing a functional scheme based on Uniform Commercial Code Art 9 in the US and the Personal Property Security Acts (PPSAs) in Canada (and now also in many other, mainly common-law, jurisdictions including Australia and New Zealand). To test views once again, the SLC consulted on such an approach but it was overwhelmingly rejected by its

consultees, who instead supported incremental reform, including retaining the current floating charge rather than introducing a parallel or replacement new revolving security interest.

We think that a UCC-9/PPSA-type scheme will continue to be viewed with little enthusiasm in Scotland unless the law of England and Wales is reformed on such a basis. This is because there is a general desire for harmonisation of commercial law and practice in the UK, rather than having laws or practices north and south of the border which are significantly different. That said, there is a particular challenge here in relation to reform of moveable transactions law, because although it is functionally commercial law, conceptually it is property law. English and Scottish property law differ fundamentally, not least because there is no law and equity divide in Scotland. In its Report the SLC has sought to make recommendations to allow businesses to transact in a way which is currently possible in England and not in Scotland, but which nonetheless is coherent in terms of Scottish property law and facilitates uniform practices and future changes. One of the Report's broad policies is to make more options available while retaining options currently used.

The SLC has also sought to prepare a draft Bill which can be passed by the Scottish Parliament under devolved legislative powers. But not all aspects of moveable transactions law are devolved. Several relevant areas, in particular legislation on registration of company charges, corporate insolvency, consumer credit and intellectual property, are reserved to the Westminster Parliament. The SLC has chosen to work within the terms of the devolved powers in order to produce a draft Bill that can be passed by the Scottish Parliament so as to optimise likely delivery of the important reforms.

Finally, the SLC has attempted to attract as much consensus on its recommendations as possible. It had an advisory group of nearly twenty individuals, including many of the leading banking lawyers in Scotland. As it worked on its Report and recommendations it engaged with key business stakeholders such as the Committee of Scottish Bankers, UK Finance, the Finance and Leasing Association, and the Federation of Small Businesses. While further discussion may be required on some points of detail in the course of implementing the SLC's recommendations,

there is broad support for the reforms which many in Scotland consider to be long overdue.

### THE PROPOSED NEW REGIMES

Volume 1 of the Report recommends reform of the law of assignment of claims. Registration would be an alternative to intimation for completion of an assignment. This would facilitate the assignment of future claims. Assignations could be registered in a new electronic register (Register of Assignations) which would be administered by Registers of Scotland (a non-Ministerial Government Department: see <https://www.ros.gov.uk/>). The Register of Assignations would be searchable electronically, primarily by reference to the assignor's details.

The rules on intimation of assignments would also be modernised. In particular, electronic intimation would be facilitated. It would be confirmed that assignments can be subject to a condition, following satisfaction of which an assignment would then take effect. It would also be made clear that in an intimation of an assignment it is possible to instruct the debtor to continue to perform to (eg pay) the assignor. Debtors who perform to the assignor in good faith, because they are unaware of the assignment, would be protected and claims arising following the assignor's insolvency would not be assigned.

Volume 2 of the Report makes recommendations in relation to the law of security over corporeal and incorporeal moveable property. A new registered "fixed" security called a "statutory pledge" would be introduced in respect of corporeal moveable property. The property would not require to be delivered to the creditor. The statutory pledge would not be available for aircraft or ships because the law already provides for special types of security rights over these assets.

The statutory pledge would also be available in respect of certain types of incorporeal moveable property. While the SLC recommends that initially the statutory pledge should be restricted to intellectual property and financial instruments, as the types of asset in respect of which there is greatest need for reform of the current law, it would be possible for the Scottish Ministers in the future to extend it to other incorporeals.

Using a statutory pledge would mean that the assets would not have to be transferred into the name of the creditor. The statutory

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pledge could be granted over future assets but would not encumber these until they became the property of the provider of the pledge. Assets acquired after commencement of the provider's insolvency would not be subject to the pledge and certain third parties acquiring pledged assets in good faith would be protected. While primarily aimed at businesses, the statutory pledge could also be granted by private individuals to raise finance against assets they already own – above a value to be prescribed by Scottish Ministers and subject to other protections.

A new register (Register of Statutory Pledges) would be set up in which statutory pledges would be registrable. Like the Register of Assignations, this would be electronic and run by Registers of Scotland. The Register of Statutory Pledges could be updated to take account of amendments, transfers and discharges of statutory pledges. The Register would be searchable electronically, primarily by reference to the details of the party that provided the security. But it would also be possible to search by reference to the unique numbers of certain assets, notably motor vehicles.

The rules on possessory pledge would be clarified too, in particular to confirm the use of constructive delivery, by intimation to a third party custodian, such as a warehouse. There would be a generally uniform enforcement regime for possessory and statutory pledges, with a range of remedies including sale, appropriation, lease and licensing. Enforcement against a private individual would require a court order.

Floating charges would remain. Agricultural charges, a little-used security which only agricultural co-operatives can grant, would be abolished but floating charges could be used instead.

Volume 3 of the Report contains a draft Moveable Transactions (Scotland) Bill which would give effect to the recommendations. The Bill is accompanied by explanatory notes.

**SOME OPPORTUNITIES**

The proposed new assignment and pledge regimes provide a great many opportunities to make transfers of claims and fixed security over corporeal moveables, intellectual property and financial instruments more efficient and, in some cases, possible in practice where currently impracticable in Scotland. The flexibility of

the new regimes should also make it more straightforward to deal in a more uniform way with both Scottish and English assets and with assets governed by further legal systems.

The following examples illustrate some of the opportunities that would become available under the new regimes:

- Invoice discounters may register a simple assignment up-front and add batches of trade receivables by electronic upload rather than by using the periodic trust mechanisms and back-up floating charges currently commonly used.
- An assignment of rents may be taken and registered up-front in relation to all present and future leases to be granted over a shopping centre without notice to tenants, with continued rental payment to the landlord and without the need for supplemental assignments on changes to tenants (as “claims” are defined under the new regime to include certain land-related claims).
- Assignment of rents from short term lettings, such as student accommodation, becomes practicable as notice to large numbers of swiftly-changing tenants is not required if the initial assignment is registered.
- Securitisation by full outright assignment of claims, such as personal loans, becomes practicable through registration up-front of a simple assignment rather than using periodic trust mechanisms (although “standard securities” over Scottish land will not become so transferable as the regime is generally restricted to moveable assets).
- Up-front “fixed charges” over operating equipment or vehicle fleets by registration of statutory pledges become a practicable alternative to finance leasing or other forms of asset finance and potentially preferable to some sale and resale back structures that carry some title risks for funders.
- Taking fixed security over intellectual property is made much easier, which should enable increased funding to become available by being secured against this increasingly important type of asset.
- Policies of some lenders against taking fixed security over Scottish shares may be reconsidered as the administrative inconvenience and real and perceived risks of going on the register of members is

removed by taking a statutory pledge.

- Fixed security over portfolios of shares becomes more practicable for Scottish shares as a simple document may be registered up-front in the Register of Statutory Pledges with shares being added automatically on acquisition by the provider of the pledge and informal identification relative to the pledge document rather than through registration of each batch of shares in the name of the secured creditor in the companies' registers of members.
- Fixed security over Scottish shares and other financial instruments which are financial collateral becomes more straightforward using possession and control mechanisms contained in financial markets securities holding structures and rules (including escrow mechanisms).

The new assignment and pledge regimes would clearly provide many further opportunities for businesses, individuals and funders, and offer flexibility for innovation, including for electronic “warehouse” financing for retail lenders, supply-chain financing, “borrowing-base” facilities and other asset-based financing.

**CONCLUSIONS**

Recent years have seen numerous jurisdictions reform their moveable transactions laws. For example, 1 January 2018 saw major new legislation come into force in Belgium. There are also growing calls for reform of English law, notably from the Financial Law Committee of the City of London Law Society and the Secured Transactions Law Reform Project. Current Scottish moveable transactions law is undoubtedly unfit for the needs of twenty-first century commerce and indeed lags considerably behind today's as-yet unreformed English law. The SLC's Report provides the basis for significant reform of Scottish law to reflect modern international standards. It is to be hoped that it will be quickly implemented. ■

**Further Reading:**

- Demystifying Scots law: Scottish aspects of debt finance transactions (2016) 1 JIBFL 38.
- LexisNexis Loan Ranger blog: Scotland to introduce new form of execution (for documents).