



Scottish Law Commission

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ISSUED ON BEHALF OF THE SCOTTISH LAW COMMISSION

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THE INSOLVENT SELLER AND THE PROTECTION OF BUYERS

Special measures to protect purchasers of land, houses, and certain other types of property are proposed in a discussion paper published today by the Scottish Law Commission.

A person seeking to buy a house or land becomes owner only on registration in the Land Register or Register of Sasines. Until that time the buyer is at risk from the possible insolvency of the seller. In particular, if the buyer pays the price to a person who is already bankrupt, or who becomes bankrupt before registration can take place, the buyer can lose both the money and the property. Such situations, though rare, have serious consequences for those affected. A court decision in the House of Lords (*Sharp v Thomson* 1997 SC(HL) 66) both highlighted the problem and sought to introduce a solution which has caused much discussion in the profession. In its *Discussion Paper on Sharp v Thomson* (No 114), published today, the Scottish Law Commission proposes that the solution introduced by *Sharp* be replaced by special legislative protection for the buyer.

THE PROBLEM

Various types of insolvency or diligence processes may come to disrupt a sale of land or other property. The seller may be sequestered. The seller's creditors may prevent the sale by inhibition or attach the land by adjudication. If the seller is a company, the company might go into receivership or liquidation, and a floating charge might attach. Usually the buyer will know if the seller is insolvent and can take appropriate steps. But not always. There can be a delay between the onset of insolvency and its registration in a public register; and there is a further delay before the information on the register appears in a search available to the buyer. This creates a blind period of a number of days during which the seller's status may be unknown to the buyer.

There are two risks in particular. One is that the buyer pays at a time when the seller is already insolvent. In that case the deed of conveyance may be invalid. The other is that the seller becomes insolvent after payment but before registration, with the result that the seller's trustee, receiver or liquidator receives (or may receive) a preferential right.

THE SOLUTION IN *SHARP*

In *Sharp v Thomson* the seller (a company) went into receivership after payment and delivery of the conveyance but before registration. Accordingly a floating charge crystallised. The solution adopted by the House of Lords was to say that, once a conveyance is delivered, the seller loses beneficial interest in the land. For the purposes at least of the legislation on floating charges, such land can no longer be regarded as the seller's property. Accordingly, it is not caught by the floating charge, and the buyer takes free of the security.

This approach has been widely criticised, as disrupting the established rules of property law without proposing a coherent replacement; as leaving much that is uncertain in an area of critical financial and economic importance; as undermining the doctrine of faith of the registers; as creating practical problems for sales by trustees, receivers and liquidators; and as providing only a partial solution to the problem identified by the case. The Scottish Law Commission accepts these criticisms and suggests that the approach taken by the House of Lords be abandoned. In its place a special legislative solution is proposed.

THE SOLUTION OF THE SCOTTISH LAW COMMISSION

The Commission makes a number of proposals of a technical nature. There are two broad aims. One is to improve the flow of information about insolvency processes to the various registers. The other is to ensure that an acquirer who registers promptly is unaffected by the insolvency of the seller. The reform is not confined to land but extends to other registered property such as company shares or certain types of intellectual property. And it applies not only to ownership but to rights in security, leases and other rights which are constituted by registration.

NOTES TO EDITORS

1. The Scottish Law Commission was set up in 1965 to promote the reform of the law of Scotland. The Chairman is the Honourable Lord Gill. The other Commissioners are currently Mr Patrick S Hodge QC, Professor Gerard Maher, Professor Kenneth G C Reid and Professor Joseph M Thomson.
2. Further information can be obtained by contacting John Dods, Scottish Law Commission, 140 Causewayside, Edinburgh EH9 1PR (Tel: 0131 668 2131, Fax: 0131 662 4900, e-mail: info@scotlawcom.gov.uk.)
3. The paper may be viewed on our website at www.scotlawcom.gov.uk or purchased from The Stationery Office Bookshops.