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Law Commission Consultation Paper No 225

Bills of Sale

1. Introduction

1.1 This response is submitted on behalf of the Financial Law Committee of the City of London Law Society (CLLS). Information about the Society and the Committee appears at the end of this paper.

1.2 We have chosen to submit a paper in which we can state our views succinctly rather than to concentrate on the response form provided. That is completed in an annexe with cross references to this paper for ease of analysis.

2. Policy Position

General Observations

2.1 We believe that the questions that arise in considering abolition of bills of sale, are as follows for each affected class, namely individuals and unincorporated businesses (in which term we include trusts holding substantial investments where the trustees are individuals):

- Over what class or classes of assets should it be possible to grant security on terms where the borrower remains in possession and control: this should reflect demand, the alternative forms of funding that would be possible and the risks of abuse;
- In respect of each such class should there be a registry and, if so, should it be public or private and how should it be funded
- Should anyone be able to be a lender or should this be limited to financiers who are regulated in some way.

2.2 The Law Commission are consulting on a proposal under which, although demand as evidenced by the use of bills of sale, seems substantially limited to the financing of vehicles already owned by the borrower ("log book loans"), with a little evidence related to security over book debts of unincorporated businesses (book debt loans), there would be a universal scheme of goods mortgages, with special rules for vehicles and a revised regime for book debt loans.

2.3 The consultation paper does not appear to evaluate:

- the costs, risks or scale of a potential simple goods mortgage scheme;
- the extent to which other available forms of credit involving goods might fulfil need and the relative cost;
- whether there are other classes of asset which should be able to be charged by individuals in the modern age (eg portfolios of shares and other securities)

We think these would be essential areas of research before proceeding to recommendation of a new scheme.

2.4 In this response we have endeavoured to make some suggestions which we believe might address needs identified by the Law Commission in different ways. We also comment on aspects of the proposals put forward, largely in the attached response form.

Lack of case for wholesale replacement of the Bills of Sale regime

2.5 We see no benefit to consumers or to the nation in general in replacing the Bills of Sale regime with a new regime in the manner proposed by the Law Commission. We do not think that the case is made out in Chapter 7 of the Report for taking this approach. While it is true that there are certain limited areas where an argument may be made that simple repeal of the Bills of Sale Acts could be a detriment to individuals or unincorporated business borrowers, we do not think that there is any case, either in terms of consumer welfare or efficiency for embarking on a costly wholesale reform of the bills of sale regime.[QI]

2.6 In the few areas where some case may be made out, then we believe that there are less cumbersome and more cost effective ways of dealing with the matter. These would be, we believe, considerably cheaper for the public purse and avoid the risk of creating a widely used regime that could inflict misery on the poorest in society, encouraging the charging of relatively low value household goods as a routine matter to a much greater extent than occurs currently.

2.7 The implications of creating a system which would facilitate the prospect that essential goods, such as cookers and refrigerators, are provided by charities or social services to alleviate an individual's poverty, yet could be mortgaged by that individual the next day to raise money and then repossessed in short order for non-payment appear not to have been considered at all.

2.8 We think that any system allowing finance to be raised in respect of goods already owned on the basis that the borrower retains possession should be subject to a substantial minimum value requirement, indexed annually, so that it keeps pace with inflation. In addition, there is a case that certain essential household goods (and possibly vital business equipment of a sole trader) should have special protection in the repossession regime in any event. [Q9] We believe, contrary to the views of the Law Commission, that there are two compelling reasons for having a minimum value:

- To ensure that the potentially oppressive use of very small value loans on a secured or "repossessible" basis is discouraged;
- To ensure that court resources are not taken up in arguments about the repossession of low value goods. Repossession, or the threat of it, can be used as an instrument of oppression, even when there would seem little practical point in the exercise, as the goods would have no more than minimal or scrap value, while having great utility to the consumer.

Dangers of allowing security to extend to non-monetary obligations.

2.9 The suggestion that security should be allowed to extend to non-monetary obligations smacks of the re-introduction of the system of trucking, bondage or even slavery – since this could make it virtually impossible ever to be free of a goods mortgage - and we think that this proposal has no place at all in legislation for a modern society. [Q5(2)]

Cost to the Public Purse – the proper role of the Courts in a modern society

2.10 From the perspective of the public purse, the proposed registration scheme and the undoubted increase in the need for court orders for repossession when the amount repaid exceeds 1/3rd of the debt would place a very substantial burden on the courts. This would apply both to the High Court, as the proposed registration body, and to the lower courts in relation to repossession orders, where, with current fee rates, there is a risk that the costs (which would fall on the borrower) may well exceed the value of the charged goods. We had understood that the policy aim

of the Ministry of Justice is to reduce the number of small value claims that might take up court time, while the proposals would undoubtedly have the opposite effect.

2.11 The job of the High Court should be focused on the administration of justice. Giving it an enhanced registry function is both incompatible with its modern role and would involve unnecessary cost burdens. The Court simply does not have the infrastructure to keep track of potentially a hugely increased number of registrations relating to relatively low value loans. This may not have mattered while Bills of Sale Acts gave rise to a small volume of registrations, but the proposals would potentially require extensive investment in registry IT, even if vehicle mortgages were dealt with in a separate private system.

2.12 This Committee's experience of use of the High Court as a registry largely relates to its function as a registry relating to administrations and liquidations of companies (many of which do not themselves require court proceedings), where we experience considerable difficulties in collecting up-to-date information. The Court Service has made it clear to us it has neither the resources or the appetite to improve its services in this regard and we see no reason why they would welcome a new and expanded role in relation to goods mortgages other than vehicle mortgages, especially as the changes would be likely to make them much more numerous than the number of non-vehicle bills of sale are currently.

2.13 We believe strongly that any existing registry functions should be either abolished or transferred from the High Court to an appropriate dedicated registry, so that the High Court can concentrate on its primary role in the administration of civil justice. The only registers it should maintain should relate to legal proceedings before the High Court.

2.14 We are concerned that the discussion at 10.65 et seq of the Consultation paper (while reflecting that the current court system is unsuitable) does not even consider use of an alternative body for non-vehicle mortgages and that none of the consultation questions actually address the suitability of the High Court as a registration body, but simply assume it.[Q20]

Summary Conclusion on Policy

2.15 We think that a policy that in practice allows only very limited grants of security by individuals has served this country well and exceptions should only be made where there is a compelling case – as with agricultural charges, or very high value items such as ships and aircraft and real estate. We therefore urge that the Law Commission recommends the abolition of bills of sale without any comprehensive replacement. This should include not just repeal of the Bills of Sales Acts, but abolition of any legal effect for bills of sale. Mere repeal of the Acts could revive prior common law.

Regulation of Lenders

2.16 We note that there does not seem to be any certainty that all lenders would be regulated. Now that there is no financial limit on consumer loans regulated under the Consumer Credit Acts, it is most likely that unregulated loans will be made by unregulated lenders. Yet it is proposed (eg Q27) that borrowers should be less protected in such cases. We believe that the proposed approach would increase the risk of oppressive behaviour by some lenders, including in family situations. Any new scheme should take great care not to create opportunities for oppression and limitation of any new form of security taking to situations where the lender is regulated and the protections of (or equivalent to) those under the Consumer Credit Acts, would be helpful in this regard.

3. Possible areas where secured loans currently facilitated by bills of sale should continue to be facilitated

Logbook Loans

3.1 We note that many consumer groups would be happy to see log book loans abolished, but we also note that over 40 thousand are entered into each year, mostly relating to already owned vehicles. This number is, however, small compared with the numbers of hire purchase and conditional sale agreements relating to new vehicles. We do not think therefore that it is a basis for creating a new form of mortgage with its own registry. It would be better to overcome any obstacles to using hire-purchase or conditional sale in those cases. For example, if there are problems with the use of hire purchase or conditional sale agreements in relation to vehicles already owned by the consumer arising from liability concerns or additional tax charges (eg VAT), the only change which may be needed to facilitate the lending by way of hire purchase or conditional sale in respect of a vehicle already owned by a consumer, would be to ensure that, after the abolition of bills of sale, an agreement to transfer ownership of a vehicle from an individual to a financier as an immediate preparatory step to it being the subject of a hire purchase or conditional sale agreement can be made on a basis which is tax and liability neutral and that the end repurchase by the consumer should similarly be tax and liability neutral. It should surely be possible to legislate to treat this step as part of the financing structure with tax and liability neutrality without creating a whole new and different legal structure with somewhat different protections for the borrower than those afforded under consumer credit legislation. One complex system for vehicle financing is quite enough and creation of a replacement for the current relatively little used alternative, seems likely to be both inefficient and costly.

3.2 We believe that there is a strong case that the protections of the Consumer Credit Acts should apply to all vehicle related loans made on terms that the financier has the right to repossess the vehicle. We also believe that such an approach is cost effective, given the relatively low number of log book loans and log book lenders as compared with the hire purchase/conditional sale market. The legal complexities of a separate system are not justified. We note that the Law Commission has some unease regarding aspects of the Consumer Credit Acts, but as they say this is a separate issue: in our view,it provides no justification for continuing or recasting a parallel system for secured vehicle loans.

3.3 As for other goods, we disagree with the Law Commission's view that there should be no minimum value for such transactions: see comments at 2.8 above. We believe that there should be a minimum value in the vehicle as the date of the transaction, which should be indexed to keep pace with inflation.

3.4 We believe that the vehicle financing industry already maintains its own records of leased and conditionally sold vehicles. While work towards instant verification of the provenance of a vehicle is welcome and would provide the best solution to the problems caused by the borrower's ostensible ownership of the financed vehicle, it seems to us it is up to the industry to decide how far they want to create a public register of financed vehicles, which would be funded by the industry, and for the Government to decide whether, as a matter of policy, such a register should require authorisation, eg from the FCA as the regulator of the industry members.[Qs 17-19]

3.5 Careful consideration should also be given to whether unregulated lenders can benefit from vehicle mortgages and, if so, with what safeguards.

Security over the book debts of unincorporated businesses

3.6 The case for improving borrowing options for small businesses is strong. In the corporate world factoring arrangements by way of outright assignment are often backed up by a floating charge over the same class of debts and the arrangements under the Bills of Sale Acts can satisfy a similar function.

3.7 We question again, however, whether the proposals take the right approach. Businesses with enough volume of book debts to justify the cost this "belt and braces" approach must be close to the size where incorporation might be advised. As the government reduces red tape for small companies, incorporation and related reporting obligations will become less onerous and the need for a separate security method for unincorporated businesses less necessary. It is certainly desirable that any method available is as close as possible to that for incorporated businesses.

3.8 We therefore suggest that sole traders and partnerships without legal personality are enabled to make a voluntary registration at Companies Registry as unincorporated businesses and that any business that has so registered should be able to create a charge over the business assets (but not the personal assets) of its sole trader or partnership on substantially the same terms and subject to the same requirements as if it were a company. This proposal would cover a wider range of assets that book debts, but could be restricted to book debts if so desired, though we doubt that this is necessary. [Q13]

3.9 By piggy-backing on the existing system for corporate charges cost and legal complication could be minimized and transparency would be improved as the Companies Registry is readily accessible.

3.10 Consideration would need to be given to the position on insolvency and whether the charged assets should be available to a trustee in bankruptcy to the same extent as similarly charged corporate assets are available to an administrator.

3.11 The comments at 2.7-2.9 above about the unsuitability of the High Court as a registry also apply to these proposals.

Security over high value assets of high net worth individuals

3.9 There is an obvious lacuna in that assets such as yachts and private planes will continue to be able to be given in security by individual owners, but, if bills of sale are abolished, not items such as valuable works of art and antiques, unless they are pledged, in which case the owner would be deprived of enjoyment of the asset. In many cases this problem may be avoided by use of a corporate ownership structure if such valuable assets have to be used to raise finance.

3.10 It does not appear from the information that the Law Commission has that bills of sale are much used in respect of such assets. It would be possible to take steps to gauge interest in the relevant business sector (eg fine art dealers and auction houses and providers of their financing schemes) in establishing an authorised register of secured financings and whether this could be set up, including consideration of what law would be appropriate to allow charges (or transfer to hire purchase/conditional sale (see 3.1 above) in respect of high value items and whether a registry was needed and could be funded, at a cost which would be reasonable to the industry and borrowers.

3.11 The case would need to be made to government that there would be a real need and an appropriate minimum value for the charged asset (not the amount of the loan) established. We do not see this system as at all suitable for rapidly depreciating or lower value household goods, but for items of substantial longer term, even if fluctuating, value.

3.12 There is a strong argument that a system of giving security over individually owned portfolios of securities (and portfolios held by trusts with individual trustees) should be considered, if there is sufficient interest from lenders.[Q6] In such a case future assets in this class should also be able to be charged. [Q10] In this case, use of records kept by the intermediaries who hold most quoted securities may provide an alternative to a registry.

4. Absolute Bills of Sale

4.1 Given the reference in the Consultation Paper to the way that absolute bills of sale might be used to shield assets from creditors or thwart a divorce settlement (2.37), we do not consider it would be appropriate to simply deregulate this form of bill of sale. Rather they should be abolished or made of no legal effect, like other bills of sale, as part of the repeal process. [Q14]

5. Issues related to the proposed new processes for Goods Mortgages

Requirement for "wet-ink" signatures

5.1 Having regard to Directive 199/93/EC on an Community Framework for Electronic Signatures and its UK implementation, the Electronic Communications Act 2000, and to the replacement of the Directive with effect from 1st July 2016 by Regulation(EU) No 910/2014 on Electronic Identification and Trust Services for electronic transactions in the internal market Section 4, especially the terms of Article 25, which will be directly effective in the United Kingdom, the requirement for wet ink signatures would be over-ridden by the requirement of these laws to recognise electronic signatures and give legal effect to documents signed in this manner. [Q11(2)]

5.2 Electronic signature methods can include the signature of a witness, so we see no problem with the requirement that the borrower's signature must be witnessed.

5.3 We believe that consumers and businesses are increasingly expecting to be able to make financial commitments by electronic means and to have confidence that they are not more open to fraud than wet-ink signatures. Domestic and international national policy favours the development of eCommerce. In addition, we are aware that Major financial institutions in the UK are already using these methods in dealing with their customers. This change in practice needs to be recognised in the Law Commission's proposals.

Unsuitablity of the High Court as a Registry

5.4 We refer to our comments at paragraphs 2.10-2.14 above.

6. About CLLS and the Financial Law Committee

The City of London Law Society (CLLS) represents approximately 14,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government Departments, often in relation to complex, multijurisdictional legal issues. The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees.

The Committee submitting this paper is made up of solicitors specialising in UK and international financial law in a number of law firms based in the City of London, who advise and act for UK and international financial institutions and businesses and for regulatory and governmental bodies on financial law matters.

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