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1 INTRODUCTION

1.1 This document is a response to Law Commission Consultation Paper 246, "*Consumer Sales Contracts - Transfer of Ownership*", which was issued on 27th July 2020 (the "**Consultation**") and the draft *Consumer Rights (Transfer of Ownership under Sale Contracts) Bill* (the "**Bill**"). Terms defined in the Consultation have the same meaning in this response.

1.2 The CLLS represents approximately 17,000 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, multi-jurisdictional legal issues. The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees. The CLLS Insolvency Law Committee, made up of solicitors who are expert in the field, has prepared the comments below in response to the Consultation. Individuals and firms represented on this Committee are set out in the Appendix.

1.3 It is noted that the Law Commission is not asking questions on the underlying policy set out in its 2016 Report, as this has already been the subject of consultation. We have therefore limited our response to a number of practical points concerning the impact of what is proposed in the Consultation on both insolvency officeholders and consumers whose claims have to be dealt with by those insolvency officeholders.

1.4 While we are not commenting on policy issues, it should be noted that the exercise of considering the impact of the proposals did repeatedly raise the question of whether their potential benefits (having regard to the limited number of creditors whose position may be improved and the expectation that they would not lead to a "significant reduction in the overall level of consumer detriment")[1] may be outweighed by potential disadvantages. This would particularly be the case if the title transfer provisions set out in the Bill created potential uncertainty in relation to the circumstances in which a creditor could make a claim under Section 75 of the Consumer Credit Act 1974 or request a Chargeback.

1.5 We have kept our comments at a high level but would be happy to discuss or expand on any of the comments made in this response, if requested.

2 How problematic is the current position for both insolvency officeholders and the consumers that they deal with?

2.1 In order to put our subsequent points into context, it may be useful to summarise how insolvency officeholders would, under the current legislation, typically deal with ownership

[1] Paragraph 5.38

issues in a retail insolvency, as there is a risk that what is proposed in the Consultation and the Bill could introduce uncertainty to an area of law and practice that is relatively well settled.

2.2 The process for resolving ownership issues is, under the current legislative regime, relatively straight-forward:-

Ascertained Goods

(a) Where there is an unconditional contract for the sale of specific goods, and nothing further needs to be done to those goods, the consumer will obtain possession of those goods by virtue of Rule 1 in Section 18 of the SGA 1979;

(b) In relation to other contracts for the sale of specific goods, the remaining Rules in Section 18 require the insolvency officeholder to check whether the consumer had received notice or had taken some other specific action (in the case of goods delivered on approval).

(c) If there is no evidence that the consumer had received such notice, or taken such action, with the result that title to the goods did not pass, the insolvency officeholder will normally remind customers that they are entitled, depending on whether they paid by credit or debit card, to make a Section 75 claim or to request a Chargeback from their card issuer. In either case, the customer normally accepts their position, having been given a clear route to obtaining repayment.

Unascertained and future goods

(a) It is suggested in Paragraph 2.32 of the Consultation that "*uncertainty surrounding the meaning of "unconditional appropriation" … makes the law difficult for.…insolvency practitioners to apply*." We are, however, not convinced that this is the case, in practice, as there seems to be a general acceptance that unascertained goods are not irrevocably committed to the contract until they are in the process of being delivered.[2]

(b) This point is important, because an insolvency officeholder will rarely be in a position, on appointment, to stop either deliveries which are already under way or deliveries which have already been arranged. They will have other immediate priorities and, in any event, they would have no reason to stop the delivery of goods which were no longer owned by the company.

(c) The current default position is therefore that those consumers who have obtained title to goods on the basis that those goods have been irrevocably committed to the contract will, in practice, normally receive those goods without any further consideration or action being required on the part of the insolvency officeholder.

While the procedure for dealing with ownership issues has the benefit of being relatively quick and transparent, we are aware of cases where the current legislative regime has resulted in very unfortunate outcomes, particularly where customers have paid in advance for big ticket items using cash or a cheque.

Our experience is, however, that such outcomes were much more common a decade ago, when the administrators of retailers such as Focus DIY had to deal with customers who had paid by cheque for new kitchens and bathrooms. There are far fewer cases of this type today,

[2] As noted in Para 3.36 of the Consultation - "*Under the existing law, ownership is unlikely to transfer until the goods have been dispatched*"

as the vast majority of creditors pay for big ticket items using credit or debit cards, encouraged to do so by publicity highlighting the protection offered to them by Section 75 of the CCA and Chargeback.

We strongly suspect, although we do not have firm evidence to support this, that the trend towards using credit and debit cards in a retail environment will be accelerated by the current pandemic, as more businesses become "cashless", and that the issue which has been identified in relation to payments in cash or by cheque will therefore become increasingly less relevant over time.

As a final point of clarification, when looking at the existing position, it is suggested that "*as insolvency practitioners owe duties to all creditors they may be inclined to err on the side of caution and instruct shop or warehouse staff not to release such property to prepaying consumers.*"[3] It is true that an administrator or liquidator may ask for further evidence before releasing goods to a customer, but they would be very aware that, as officers of the court, they must act fairly and cannot disregard the statutory framework. They would also be aware of the risk of incurring personal liability if they prevented consumers from obtaining goods which belonged to them. Erring on the side of caution could therefore result in goods being released to prepaying customers, where there was genuine doubt as to the legal position.

3 The risk of the proposals resulting in significant additional insolvency costs

3.1 Consultation Question 32 states that "*we estimate that the proposed rules in the draft Bill would result in only a minimal increase in time spent by insolvency practitioners in determining whether ownership of goods has transferred to a consumer in the event of insolvency*."

3.2 The Consultation then goes on to assume that the assessment of whether ownership has transferred would "*likely involve a desk-based exercise, including a review of the retailer's records and discussions with employees in the retailer's shops and warehouses as to the status of goods they are holding*."[4]

3.3 We do not think that this correctly reflects the position, at least in larger retail insolvencies, as:-

(a) A significant number of stores may be closed immediately, if they were not trading profitably;

(b) Employees may not be kept on, either because the store in which they worked is being closed or because the administrator does not want to "adopt" their contract of employment;

(c) Key staff may decide to leave, realising that they will only continue to be employed for a limited period of time;

(d) Stock may have to be moved rapidly out of any stores and warehouses that the administrator or liquidator is not planning to use, a process which could result in labels and other means of identification being lost in transit;

[3] Paragraph 2.18

[4] Paragraph 5.28

(e) There is often a lack of accurate records, either as a result of staffing cuts to reduce overheads, operational restructurings aimed at reducing costs or just corners being cut immediately pre-insolvency; and

(f) The goods in question may have disappeared. Employees and customers may exercise "self-help" remedies, when told that the retailer has gone into an insolvency procedure and will not pay them or otherwise meet its obligations, taking the view that they will help themselves to goods of equivalent value to the amount owed to them.

3.4 Difficulties with obtaining accurate information could be exacerbated by a complex fact pattern. This can be illustrated by the example of buying a sofa from a retailer, where a sofa of the relevant type was identified at the warehouse and then labelled and set aside to be delivered to the relevant customer. The delivery schedules might then change, as the original customer could not take delivery when planned, with the result that the sofa was sent to someone else instead. Analysing the legal position under the proposed new legislation could be problematic, even if the contractual position was clear, as an administrator or liquidator would need to establish whether making such swaps was sufficiently common practice to rebut the argument that the labelling was intended to be permanent. Reaching a conclusion on this point may not be straight-forward if the relevant staff were no longer employed by the company.

3.5 It would also be necessary to deal with individual consumers one by one. In some cases, the additional time required to administer large quantities of consumer title claims might slow down the insolvency proceedings considerably, for example requiring warehouses to be maintained and staff employed for longer than is currently the case, adding significantly to the cost of the process.

3.6 The position when investigating whether title to goods, and particularly unascertained goods, had transferred under the proposed new legislation would, we believe, be analogous to the existing process followed by insolvency officeholders when dealing with retention of title claims, as this also requires a mixture of factual and contractual analysis. Our experience is that dealing with ROT claims is often a time consuming and expensive process which requires the attention of a significant number of the insolvency officeholder's staff, as well as the provision of external legal advice.

3.7 While a similar approach may be taken, there is a risk that the process for investigating whether title to goods had transferred could prove more expensive than the current process for dealing with ROT claims, as it is normally possible to do a deal with ROT creditors, thereby avoiding spending too much time in reaching a final conclusion. This would not be the case with transfer of title claims, as the position would normally be a binary one – either the customer gets their goods or they don't.

3.8 We would therefore, for the reasons outlined above, disagree with the conclusion that it would not take significantly longer for insolvency practitioners to assess ownership of goods under the proposed new legislation than it does under the existing rules in the Sale of Goods Act 1979.[5]

[5] Paragraph 5.29

4 Potential impact of the Bill on Section 75 and Chargeback claims

4.1 As noted above, and as recognised in the Consultation, the ability to make a Section 75 claim or to request a Chargeback is extremely important to consumers in a retail insolvency context.

4.2 There would be very significant concerns if what is proposed could result in consumers being worse off, either losing the ability to recover the purchase price from a card provider or finding it much more difficult to make such a claim. The rights of consumers as a whole (most of whom pay by debit or credit card) should not be prejudiced in order to protect an increasingly small minority who prepay using cash or a cheque.

4.3 In this context, the Consultation rightly asks:-

(a) How customers would be treated if they would prefer to receive a refund of prepayments rather than the goods themselves, even where ownership of goods had already transferred to them? This could be a particularly important consideration where the customer would be better off making a claim for repayment under their credit card than having to arrange to pick up kitchen units from a warehouse 150 miles away; and

(b) Whether the Section 75 and Chargeback regimes would reimburse the costs of paying outstanding storage costs, or the costs of arranging for goods to be collected from a warehouse.

4.4 We would raise the following additional points:-

(a) **Evidential requirements**: Would the consumer be required to establish the legal position as to title to the goods before making a Section 75 or Chargeback claim?

(b) **Insurance:** The Consultation provides that, as is currently the case under the CRA 2015, goods would remain at the company's risk until they come into the physical possession of the consumer or a person identified by the consumer to take possession of the goods.[6] This raises the question of what would happen if the business in question failed to maintain adequate insurance cover, with the result that goods owned by the consumer were destroyed in a fire or stolen. The consumer would clearly have a (potentially worthless) claim against the company in such circumstances, but it would be essential to ensure that a Section 75 or Chargeback claims could be pursued in such circumstances.

(c) **Warehouse liens**: It is assumed that the consumer would be bound by warehouse liens in most cases, as the lien will almost always be in existence before the transfer of ownership occurs.[7] In such cases, it seems that the consumer could potentially be in a significantly worse position under the proposed new legislation, if the retailer owed a large amount to the warehouse, unless the consumer was definitely entitled to make a Section 75/Chargeback claim in such circumstances.

4.5 It is important, from the point of view of all stakeholders, that there is clarity on these points and that there is no risk that transferring title to goods at an earlier stage in the process could result in consumers having a lower level of protection under the Section 75 and Chargeback regimes than is currently the case.

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[6] Paragraph 3.9

[7] Paragraph 3.126

4.6 It is not the role of this Committee to provide legal advice in relation to the interpretation of existing legislation, particularly where there may be a range of views, but we do note that the Consultation appears to accept that the position may not be entirely certain on a number of points:-

(a) "*Where the consumer has chosen to treat the sales contract as at an end under the CRA 2015 because of the retailer's refusal to deliver the goods, and the consumer then claims reimbursement, there is a strong argument that the claim for reimbursement is "in respect of a breach of contract… A section 75 claim should therefore be possible in this situation*."[8] [our emphasis]]

(b) *"If the consumer decides they want the goods and arranges for pick up or delivery of them, we think that the consumer could recover these costs (where they are reasonable costs) under section 75*."[9] [our emphasis]]

This uncertainty appears to be reflected in Consultation questions 12 and 13

4.7 In order to reduce the risk of their being any uncertainty in this area, we would strongly suggest that the industry code of best practice produced by the UK Cards Association, and any relevant equivalents, should make it clear that such costs should be covered by a Section 75 or Chargeback claim and that the introduction of the changes set out in the Bill should have no impact on a consumer's ability to make a claim for goods that they do not receive.

5 Potential problems which insolvency officeholders may face when dealing with consumers

It is important, in order to minimise the time spent explaining the situation to individual creditors, and thus to avoid any unnecessary resulting costs, that the rules as to ownership should be clear, consistent, fair and logical. There is a risk that certain aspects of what is proposed may appear inconsistent or unfair. Specifically:-

(a) **Apparent randomness**: As noted in the Consultation, "*It may be a source of frustration for consumers that the transfer of ownership depends on events and circumstances entirely within the retailer's control, such as labelling*".[10] This frustration may be increased by the fact that consumers, and the insolvency officeholder's staff dealing with them, may not have access to the information required to work out the consumer's legal position; and

(b) **Differences in recovery position between in person purchases and on-line purchases.** The proposals in the Consultation may not apply to on-line purchases as (i) the proposed rules will, as noted in the Consultation, apply only to contracts governed by English law[11] and (ii) even in those cases where English law does apply, many internet retailers provide in their standard terms that a contract will only be entered into once the goods in question are ready for delivery.

This may create a two tier system, particularly where a retailer has both physical stores and an on-line offering, as the creditor's position may depend on which

[8] Paragraph 3.96

[9] Paragraph 3.100

[10] Paragraph 5.37

[11] Paragraph 3.8

method they used to purchase a specific product. Creditors may not understand why this should be the case.

6 Impact on security arrangements

6.1 It is noted in the Consultation that "*the proposed rules in the draft Bill may reduce the effectiveness of the security held by the retailers' other creditors*".[12] The prejudiced parties include (i) secured lenders with a floating charge or stock financing security and (ii) suppliers relying on ROT provisions.

6.2 While it is true that, in many cases, the reallocation of risk envisaged by the Consultation will not, in itself, be sufficient to cause suppliers to change their terms of business, or to alter the terms on which banks provide new funding, it is important to consider what is being proposed in its wider commercial context.

6.3 In this respect, it should be borne in mind that there have been an increasing number of statutory amendments which dilute the effectiveness of floating charges, most recently the reintroduction of crown preference, with HMRC becoming a secondary preferential creditor with effect from 1st December. When introducing any measure that further erodes the benefit of taking a floating charge, it is necessary to consider the cumulative effect of all such erosions, as these may, eventually, have an impact on the price of lending.

6.4 Similarly, the draft Bill will have a detrimental impact on the effectiveness of ROT clauses, by reducing the time during which they would have effect. The impact of this will vary, depending on the exact fact pattern, but, once again, this impact needs to be viewed in its wider commercial context, as suppliers are currently adjusting to restrictions implemented in the Corporate Insolvency and Governance Act which prevent them from being able to rely on insolvency related termination rights. If their ability to rely on ROT clauses is also limited, there may eventually be pricing consequences that feed through to consumers, to reflect the increased insolvency-related risks that suppliers are being asked to take.

POINT OF CONTACT

Should you have any queries or require any clarifications in respect of our response or any aspect of this letter, please feel free to contact me.

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Other members of the Insolvency Law Committee are listed here:

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[12] Paragraph 5.17