Introduction

1. This paper has been produced by the Working Group A (WGA) of the Secured Transactions Law Reform Project. Its purpose is to consider how the law could be improved in relation to the persons who can provide registrable interests. It summarises the work done by the WGA since February 2012. Views presented in this paper are provisional and open to further discussion. In addition, they are expressed in members’ private capacities and should not be attributed to any institution or organization where members work.

2. Under the current law registration of security interests is spread over different registers depending on who grants security. Security interests are registrable in the Companies House when granted by a registered company or a limited liability partnership (LLP) in the form of a charge unless the charge falls within one of the few exceptions specified in Companies Act 2006, s 859A. Security interests granted in writing by individuals or groups of individuals, including unincorporated businesses, must comply with Bills of Sale Acts 1878-1891 and are registered in paper form at High Court. The register is neither easily searchable nor reliable due to errors. In addition, the Acts are highly technical and the slightest slip in complying with the requirements of the statutory form or other formalities can result in the invalidity of the security or even of the personal covenants contained in the bill of sale.

3. In our view Bills of Sale Acts (the Acts) condemn borrowers to unnecessary formalities (“red tape”) with unacceptably harsh consequences for lack of compliance, resulting in costly and inflexible credit. The Acts fail to provide transparency of registration of security where it is much needed. In addition, we think that the disparity in the treatment of individuals on one hand and companies on the other is not justifiable in a modern economy: both may be involved in running a business and should benefit from the same business opportunities, including access to secured credit. We recommend that the same system of registration of security should be available to both companies and LLPs and to individuals who are not consumers.

4. In our view there is no reason why security provided by all individuals, including consumers, could not be dealt with comprehensively in the new regime governing secured transactions. However, our discussions to date have thus far not extended to consumers as we have recognised that separate issues arise in relation to consumer
credit regulation. Hence, the scope of this paper does not extend to consumers. Similarly, our recommendations for the time being do not extend to bodies corporate other than companies and LLPs (for example, bodies incorporated by Act of Parliament or Royal Charter, public benefit corporations such as NHS foundation trusts or industrial and providential societies) or to foreign companies. Registration of security interests by these bodies may also be considered at a later stage.

5. This paper first outlines the problems with the current law that governs security granted by individuals. It then proceeds to identify the categories of individual to whom the system of registration would apply and finally, it suggests ways in which such a system could work in the future.

**Shortcomings of the current law governing secured lending to individuals**

6. The Bills of Sale Acts 1878-1891 have been criticised for many years for the technical pitfalls they have created. They first attracted negative judicial commentary just a few years after the introduction of the Bills of Sale Act (1878) Amendment Act 1882. The Crowther Report in 1971 recommended repeal of the Acts whilst the Law Commission Consultation Paper in 2002 concluded that serious consideration should be given to the reform of this area. In December 2009 BIS proposed banning the use of bills of sale (BIS 2009 Consultation Paper “A Better Deal for Consumers”) based on the need for wider protection and encouragement of responsible lending practices. No legislative reform took place. Instead, a voluntary code of practice for logbook loan companies was adopted. While we note that this area is subject to debate and a new consultation at the Law Commission opened on 9th September 2015, this paper does not deal directly with issues raised in the consultation.

7. Historically, bills of sale have been used by commercial enterprises to purchase ships, cargo or stock, not to provide security in goods. They were arguably never suited as a security interest vehicle.

8. The Acts are highly technical and the slightest slip in complying with the requirements of the statutory form or other formalities can result in the invalidity of the security or even of the personal covenants contained in the bill of sale. Moreover, with some exceptions the Acts prohibit the grant of security in future property.

9. Security in the form of a bill of sale is less flexible and more onerous than security granted by companies. The restrictions imposed by the Acts are as follows.

a. There are strict and complex (unclear) formalities for a security bill (prescribed in Schedule 1 of the 1882 Act), lack of which causes invalidity of security, even as between parties (1882 Act, s 9). The complex and antiquated language used in Bills of Sale Acts makes it difficult to understand the terms, even for solicitors (see e.g. *Chapman v Wilson* [2010] EWHC 1746 (Ch), where a document drafted by a solicitor was held invalid for lack of formality). By contrast, there are no formalities for creation of security by companies. The presence of formalities poses risk for the lenders that security is not created, which might influence their decision whether or not to lend against a bill of sale.
b. The Acts prohibit granting security in future assets (except growing crops) as security is void against everyone except the grantor unless goods covered in the bill are specifically listed in the schedule (1882 Act, ss 4, 5). If future goods are not sufficiently described in the prescribed form, the bill of sale will be void against the debtor too. This is also usually seen as precluding unincorporated businesses from obtaining a floating charge, which is available in relation to companies.

c. Registration of bill of sale with High Court within 7 clear days is necessary for its validity. Repayment of the debt does not extinguish the bill automatically as a satisfaction certificate must be issued. Apparently in practice it is almost impossible to match bills with the certificates due to physical cataloguing and recording problems.

d. Register of bills of sale maintained by High Court is paper-based, difficult to search and lacks transparency.

e. Although the Acts apply to security granted in goods, the registration requirement extends to general assignment of book debts by an unincorporated business by virtue of s 344 of the Insolvency Act. There is no possibility to register security in other assets. Such protection is available to lenders when lending to companies.

f. Insofar as priority rule is concerned, the priority is looked at by the date of registration. There may be a gap between creation of security and its registration, when the lender is at risk (it is not clear what the position is). Similar problem exists in relation to companies. Priority issues are discussed separately by a specialist group, Working Group B of the Project.

10. For the reasons listed above the ability to borrow by unincorporated entities is limited and borrowing is probably more costly than secured borrowing by companies. A restricted ability to borrow creates an unnecessary pressure to incorporate. There seems to be no reason for difference in treatment between lending to corporate and incorporate debtors (this was noted in the Diamond report, “A Review of Security Interests in Property” 1989, para 16.15). In our view Bills of Sale Acts should be repealed and replaced with an alternative system of registration of security.

11. In the section that follows, we explain which categories of individual should be brought with the scheme of registration available for companies and with respect to whom Bills of Sale Acts should be repealed as soon as the alternative scheme is in place.

Individuals to be brought within the registration of security scheme (non-consumers)

12. Individuals creating security when entering into consumer credit agreement or individuals entering into consumer hire agreements fall within the ambit of the regulation under Consumer Credit Act 1974 (CCA) and Financial Services and Markets Act 2000 (Regulated Activities) Order 2001/544 (referred to later as RAO), as amended recently by the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No.2) Order 2013/1881. The regulation covers private consumers, sole traders, small partnerships, including partnerships consisting of two or three persons not all of whom are bodies corporate, and unincorporated bodies of persons, which do not consist entirely of bodies corporate and is not a partnership (s 189(1) CCA), for example unincorporated clubs, charities or trade unions. Regulation of consumer credit
and hire agreements has undergone some changes that came into force on 1st April 2014. As of that date the regulation was transferred to Financial Conduct Authority (FCA) from the Office of Fair Trading. Regulation of consumer agreements raises separate issues than agreements in a non-consumer context, which is why we have excluded from our discussions regulated (consumer) agreements for the time being, recognising that this position may require reconsideration in due course.

13. Under certain circumstances lending to individuals qualifies for exemption from the consumer regulation, as specified in RAO. As of 1st April 2014, the exempted agreements are: certain credit agreements (as specified below), certain hire agreements (as specified below) and agreements relating to supply of gas, electricity or water where the owner is a body corporate.

- Credit agreements are exempted from regulation where:
  - they are entered for business purpose (RAO, art 60C);
  - the borrower is a high net worth individual (RAO, art 60H);
  - they are secured by mortgage to purchase land for non-residential purposes (RAO, art 60D);
  - the lender is a local authority or a body specified by the FCA, the credit agreement relates to purchase of land and is secured by a mortgage on that land and (RAO, art 60E);
  - the lender is a credit union and the rate of the total charge for the credit does not exceed a specified threshold provided some other conditions are met (RAO, art 60G);
  - they fall within specified category of credit agreement (such as an agreement to supply fixed-sum credit; an agreement for running-account credit; financing purchase of land financing a premium under a contract of insurance, either relation to land or life insurance) and the number of repayments is limited to four or fewer, depending on the type of agreement (RAO, art 60F).

- Hire agreements are exempted from regulation where:
  - they are entered for business purpose (RAO, art 60O);
  - the hirer is a high net worth individual (RAO, art 60Q).

14. Of these exemptions, the problems arising under Bills of Sale Acts (discussed in paras 6-11) are most likely to arise in relation to secured credit agreements and hire agreements entered into for business purposes or by high net worth borrowers or hirers. The other exempted agreements fall outside of the Bills of Sale Acts because they either involve land or otherwise are not likely to involve a security in a personal chattel. Our recommendations for the time being focus on bringing within the registration scheme those individuals, or groups of individuals, who borrow or hire for business purposes and the high net worth individuals; hence the need to discuss these two categories in more detail.

**Lending for business purpose**

15. There are three categories of exemptions in relation to business lending following the amendments that came into force on 1st April 2014:

- First, exemption applies to agreements by which the lender provides the borrower with credit exceeding £25,000 and the agreement is entered into by the borrower wholly or predominantly for the purposes of a business carried on, or intended to be carried on, by the borrower (RAO, art 60C(3)).
• Second, exemption applies to agreements even where the lender provides the borrower with credit of £25,000 or less if it is wholly for business purpose entered for business purpose and the agreement is a green deal plan within the meaning of Energy Act 2011, s1, that is an arrangement made by the occupier or owner of a property for a person to make energy efficiency improvements to the property (RAO, art 60C(4)).

• Third, an agreement is exempt if it is made in connection with trade in goods or services abroad or between the UK and a country outside the UK and the credit is provided to the borrower in the course of a business carried on by the borrower (RAO, art 60C(8)).

16. In relation to the first two exempted agreements, it is presumed that the agreement is for a business purpose from a declaration made by the borrower that the agreement is entered into by him/her wholly (or predominantly) for the purposes of a business carried on, or intended to be carried on, by him/her, provided that the agreement complies with rules set out by the FCA in the Consumer Credit sourcebook (CONC). These rules relate primarily to the form and content of the declaration and the credit agreement (FCA CONC App 1.4). The term “business” is defined widely under CCA as including profession or trade except where a person occasionally enters into transactions belonging to a business (s189(1) and (2) CCA). The presumption does not apply if, when the agreement is entered into, the lender, or a person acting on lender’s behalf, knows or has reasonable cause to suspect that the borrower does not enter into the agreement wholly (or predominantly) for business purpose. For example, if a small trader buys on credit through his business books a van worth more than £25,000, the agreement is not regulated if the van is intended and declared predominantly for a business purpose. If the trader declares business purpose but the lender knows that the car is intended for private purposes, the agreement falls within the scope of regulated agreements.

17. We do not presently advocate any change to the current rules on determining business purpose (self-declaration with the residual role of lender’s or owner’s knowledge). We think that the current law strikes a balance between freedom of an individual to decide whether to be exempted from the regulation where the agreement is for a business purpose and the risk of exploitation of the individual’s position by the lender or the owner. We are, however, open to further discussion on this point.

High net worth borrowers or hirers

18. Exempted agreements include credit agreements relating to high net worth borrowers for loans secured on land or exceeding £60,260 (€75,000) or hire agreements where the hirer is a high net worth individual. The borrower must be an individual, who makes a declaration to forego the protection and remedies available for regulated agreements as well as a statement in relation to his/her income or assets. A high-net-worth individual is an individual who received at least £150,000 net (total) income in the previous financial year, or had net assets worth at least £500,000 throughout that year (FCA Consumer Credit sourcebook, CONC App 1.4).

Identifying individuals for the purposes of registration of security

19. If our recommendation to bring individuals within the scheme of registration of security is followed, it is necessary to consider how individuals could be identified with clarity and certainty. Prospective creditors searching the register will want to access...
unambiguous information regarding any existing security granted by the individual whom they are looking to finance. We recognise that there is a risk of ambiguity, for example where two individuals correspond to one identifier. However, we think that a carefully designed system can minimize this risk. Even if this risk cannot be eliminated completely, we do not think that it outweighs the benefits of extending the registration scheme to individuals. The current law offers very little flexibility and has numerous shortcomings, as outlined in paras 6-11. What follows in the paragraphs below does not purport to deal with the question of design of the register, which we discuss in a separate paper, but aims to show how the problems with identification of individuals could be overcome.

20. There are two possible approaches to dealing with the risk of ambiguity: to put the burden on the person filing for registration to ascertain and file under the correct identifier or to put the burden on searchers to identify and search against all possible minor errors. We advocate the former approach because in our view it is more likely than the latter to promote transparency, clarity and reliability on registers.

21. The possible identifiers of individuals are as follows: names, VAT numbers, national insurance numbers or some other number such as personal identification number, which may be available in relation to some foreign individuals. We describe each in more detail below.

22. In our view, identity of an individual could be ascertained using a combination of two or more identifiers. This would increase the certainty of correct identification of a person. Searches in the register should also be possible against any of the identifiers accepted in law. For example, if security could be registered against an individual’s name and their VAT number, the register could then be searched against both the name and the VAT number. In an electronic register, the possibility of setting up a functionality of searches against multiple identifiers is not likely to be costly.

Name of the individual

23. One possible identifier is the name of the individual. This is a convenient and readily available identifier because every person has one. Names of individuals are used as identifiers in other jurisdictions, for example under Article 9 of the Uniform Commercial Code in the USA. When adopting this approach, it is necessary to deal with problems of individuals having the same names or individuals changing names (for example, upon marriage) as well as the issue of how to ascertain the correct name, that is which documents to accept as proof of a person’s name. None of these issues is insurmountable. These are technical issues that would be dealt with in due course when designing the functioning of the register.

24. In case of partnerships, we recommend that security should be registered against the name of one or more of the partners, not against the name of the partnership as the latter may change without any record.

VAT number

25. This option is viable for businesses, which correspond to individuals and groups of individuals falling within articles 60C and 60O of ROA. The following entities can register for VAT if they are in business: an individual, a partnership, a company, a club,
an association, a charity, any other organization or group of people acting under a particular name. Under current rules (as of end of June 2014) registration for VAT is compulsory if the turnover of VAT taxable goods and services supplied within the UK for the previous 12 months is more than the registration threshold (currently £81,000). Below this threshold registration is voluntary.

26. Not everyone will have a VAT number or want to register for it. Some are not eligible for VAT at all: a business that sells only goods or services that are exempt from VAT cannot register for VAT. Goods and services exempt from VAT include insurance and finance, education and training, charitable fund-raising events. Individuals engaged in such activities may nevertheless qualify as businesses for the purposes of ROA. In such cases registration of security could take place against the names of the individuals and, for example, a national insurance number.

National insurance number

27. In many instances in the UK the national insurance (NI) number functions as one’s personal identification number, unique to a person. Once assigned to a person, NI number does not change. A register of security interests searchable by individual’s names and verifiable by NI number could therefore be a feasible solution to the problem of identification.

28. The issue associated with this option is that the NI number may be seen as “personal data”: if a living individual can be identified from that data, a possible issue of data protection may arise under Data Protection Act 1998. We also recognise that there is some risk of false NI numbers in circulation but we do not think that the risks outweigh the benefits of introducing the registration scheme to individuals. Foreign nationals, who do not permanently work in the UK, are not likely to have a NI number.

Other numbers

29. Foreign individuals from some countries are issued with a personal identification number in their home country, shown in national ID cards, passports, driving licences and other documentation. These numbers are unique to a person and do not change even if the documents are replaced throughout a person’s lifetime. Such personal identification numbers could be used as identifiers in relation to the foreign individuals should the scheme extend to them.

30. Another option would be to give individuals, whether domestic or not, a possibility to register voluntarily for an entirely new personal identification number, which could be used in order to register a security interest (voluntary registration of individuals by a new number). This number could then be used to extend the company registration system to unincorporated businesses, as has been done with limited liability partnerships.

Conclusion

31. In our view registration of security in an electronic, transparent and readily searchable register should be open not only to companies and LLPs but also to individuals and groups of individuals, including unincorporated businesses. Bills of Sale Acts 1878-1891 fail to provide such registration. The Acts are also antiquated and fraught with difficulties to such an extent that they cannot even be contemplated as a platform for
reform. They should be repealed. Once repealed, individuals should be brought within a scheme of registration of security that would also be available to corporate bodies.

32. We recognise that many individuals providing security for credit enter into consumer agreements that are heavily regulated. The regulation aims to protect consumers but it does not eliminate the problems associated with the Bills of Sale Acts, which apply to bills of security granted by individuals, irrespective of whether they are consumers or not. However, we also recognise that consumer credit (including consumer secured credit) raises different issues than secured credit in a non-consumer context. For that reason, we decided to exclude from our discussions consumer credit.

33. In this paper we have identified circumstances when individuals fall outside consumer regulation in relation to secured finance. These are: individuals or groups of individuals entering credit or hire agreements for business purpose and individuals who are high net worth borrowers or hirers. We recommend that these categories of person be brought within the same scheme of registration of security as is available to companies. Lenders looking to extend credit to such individuals ought to be able to search quickly and electronically whether any encumbrances exist against such individuals. This will promote transparency.

34. Bringing individuals within the scheme of registration raises a problem of finding a unique identifier of the individual. We explored different options and concluded that a combination of two (or possibly more) of the following identifiers should be in place depending on the type of individual: individual’s name, VAT number, national insurance number, personal identification number (currently available in relation to some foreign individuals).

35. Although this paper did not discuss security granted by consumers, we think that the reform of secured transactions law ought to be comprehensive and ought to extend to all individuals.