

**THE REGISTRATION OF  
COMPANIES' SECURITY INTERESTS (COMPANY CHARGES)**

**A CONSULTATION DOCUMENT**

**THE ECONOMIC IMPACT OF  
THE LAW COMMISSIONS' PROPOSALS**

**JULY 2005**

## THE REGISTRATION OF COMPANIES' SECURITY INTERESTS (COMPANY CHARGES)

The Government is seeking views on the impact, cost and benefits of possible changes to the law relating to companies' security interests.

### The Law Commissions' Reports

Following consultation, the Scottish Law Commission published in September 2004, their "Report on Registration of Rights in Security by Companies" (Scot Law Com No.197, [www.scotlawcom.gov.uk](http://www.scotlawcom.gov.uk)) with their recommendations for changes to the law relating to the registration and priority of rights in security granted by companies. A summary of their report is included in this paper together with their draft legislative provisions. The Scottish provisions might be included in the Company Law Reform Bill when it is introduced during the current Parliamentary session. Alternatively, the Scottish Parliament could legislate on the devolved aspects of the package. It would not, however, be possible for devolved matters to be the subject of secondary legislation made under a power provided in the Company Law Reform Bill.

The Law Commission plan to publish their report on Company Security Interests in August 2005. It will be available on their website [www.lawcom.gov.uk](http://www.lawcom.gov.uk). The report will include draft regulations which might be implemented through a power taken in the Company Law Reform Bill. Therefore the Law Commission have made available both the draft regulations and an explanatory summary in advance of the publication of their report so that this Regulatory Impact Assessment can be completed before the introduction of the Company Law Reform Bill.

Both Law Commissions' recommendations require new systems to be put into place. Implementation of their recommendations would not be as soon as the Bill is enacted. It is not planned to make any Regulations or otherwise bring any changes into force before 2007. Therefore comments on the detail of the draft Regulations are not subject to the same deadline as for comments on the alternative options.

It would be possible to implement all or some of either Commission's recommendations. If stakeholders consider that some of the recommendations should be implemented but that the costs of implementing others would not be justified by the likely benefit of doing so, they are asked to identify the particular recommendations they would not wish to see implemented and to explain why.

Three options are described in this paper.

- |          |   |
|----------|---|
| Option 1 | Do nothing  |
| Option 2 | Implement either or both Law Commissions' recommendations |
| Option 3 | Improve current scheme for England and Wales              |

The questions that we would like you to consider for each option are:

- What would be the recurring costs to you?
- What would be the one-off costs to you?
- What would be the benefits to you?
- What would be the wider impact?

There may also be further matters that you would like to raise as a result of these proposals. The Government is interested in your views. **The closing date for comments is 7 October 2005**, but earlier comments would be helpful.

Please respond by email to:

[companylawreform@dti.gsi.gov.uk](mailto:companylawreform@dti.gsi.gov.uk)

If you prefer, you may write to:

Anne Scrope,  
Corporate Law and Governance, Department of Trade and Industry  
Bay 558, 1 Victoria Street, London SW1H 0ET  
Tel: 020 7215 2194; Fax: 020 7215 0235

### **Confidentiality & Data Protection**

Your response may be made public by the DTI. If you do not want all or part of your response or name made public, please state this clearly in the response. Any confidentiality disclaimer that may be generated by your organisation's IT system or included as a general statement in your fax cover sheet will be taken to apply only to information in your response for which confidentiality has been requested.

Information provided in response to this consultation, including personal information, may be subject to publication or disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want other information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

The Department will process your personal data in accordance with the DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties

## **Code of Practice on Consultation**

A copy of the Code of Practice on Consultation is in Annex E. If you have comments or complaints about the way this consultation has been conducted, these should be sent to:

Nick van Benschoten, Consultation Co-ordinator  
Better Regulation Team, Department of Trade and Industry  
1 Victoria Street, London SW1H 0ET

Email: [Nick.vanbenschoten@dti.gsi.gov.uk](mailto:Nick.vanbenschoten@dti.gsi.gov.uk)

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**THE REGISTRATION OF  
COMPANIES' SECURITY INTERESTS (COMPANY CHARGES)**

**REGULATORY IMPACT ASSESSMENT**

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## PARTIAL REGULATORY IMPACT ASSESSMENT

### ON PROPOSALS FOR

### THE REGISTRATION OF COMPANIES' SECURITY INTERESTS (COMPANY CHARGES)

#### 1 Proposal

To reform the law relating to the registration and priority of companies' security interests (commonly called company charges).

#### 2 Purpose and intended effect

Reform of the system for the registration and priority of company charges

##### (i) Objective

2.1. The primary objective is to facilitate company borrowing for the benefit of both creditors and debtors and hence the whole economy.

2.2. Further objectives are:

- to make information about companies' secured borrowing easily available to assist, in particular, their creditors and potential creditors;
- to prevent any difficulties arising from differences between Scots law and English law.

2.3. **Devolution:** Registration of company security interests involves both matters that are reserved to Westminster and those that are devolved to the Scottish Parliament. Responsibility for company law lies with the Secretary of State for Trade and Industry. This covers any requirement on companies to file information at Companies House. Property law is devolved to the Scottish Parliament. This means that the law relating to the creation of security interests, including their registration for that purpose and their relative priority, is devolved.

##### (ii) Background

2.4. Commercial lenders routinely protect themselves against the risk of their borrowers' insolvency by taking security over the company's assets. The main risk to a lender, whether or not secured, is that unknown to him some other lender has a prior claim to an asset. A system for the compulsory public registration of security over companies' assets is essential to minimise this risk.

2.5. Over the last 50 years, the system for registering company charges has been the subject of several fundamental reviews. However the current schemes for England and Wales and for Scotland are basically the same as that introduced in 1900 for companies incorporated in England and Wales. Under these schemes, registrable charges are valid against other creditors or, in the event of the company's insolvency, against an administrator or liquidator only if they were duly registered. This "sanction of invalidity" is extremely effective: it means that it is in the commercial interest of lenders to ensure that the charge is registered within the statutory time limit after the transaction that created the charge.

2.6. This is a complex area of law. There are many important differences between the law of rights in security and the underlying law of property in England and Wales and in Scotland. In particular:

- under English law, companies' ability to borrow is greatly enhanced by their being able to offer security over either all their assets or over specified assets. Charges are a form of security where, so long as it is solvent, the borrower retains control of the asset. If the charge is "fixed", the lender's consent is required before the borrower can sell the charged asset; under a "floating charge", the borrower can sell the charged assets during the normal course of business.
- the forms of fixed security available to companies under Scots law is more limited than under English law. A fixed security may be created over land by registration in the Land or Sasine Register of a standard security, but in order to create a fixed security over moveable property (whether tangible or intangible) the debtor must part with possession. In order to mitigate these limitations the concept of a floating charge was introduced into Scots law by statute in 1961, when a requirement to register particulars of floating charges and other rights in security over certain types of property was also introduced.

(iii) **Rationale for Government intervention**

2.7. The system for registration of company charges is needed to address the following risks:

- the concealment of secured credit with markets being misled by the apparent unencumbered ownership by companies of assets which in fact are encumbered in favour of prior creditors;
- uncertainty over the rights of secured parties in the event of the borrower's insolvency;
- uncertainty over the rights of those who buy assets that are subject to security interests.

These risks are present particularly under English law; Scots law generally does not allow secret or concealed security.

2. 8. A security right constituted in accordance with the law of one legal system may not be recognised by another legal system, particularly when it is in conflict with another security right effective under the latter system or with the rights of a purchaser or acquirer under that system. There are thus potential risks arising from the difference in underlying property law between Scotland on the one hand and England and Wales on the other may also give rise to problems relating to:

**Validity**, ie whether a charge is recognised in both jurisdictions.

**Priority**, ie whether a charge that ranks before another in one jurisdiction also does so in the other.

2. 9. Differences in the rules for registration of security interests between the two jurisdictions and in the information available on the public record at Companies House may confuse users of the systems.

2. 10. The Company Law Review sought views on improving the present system, primarily by simplifying procedures and refining definitions. They reported that those who responded to their consultation were almost unanimous in agreeing that some system was still needed for the registration of company charges. (The only disagreement was as to whether the system was also needed in Scotland.) The Company Law Review noted that, while there was little consensus on any of the main issues, convincing arguments in favour of radical change had been advanced.

2. 11. In the light of this consultation, they developed a provisional set of proposals which differed significantly from those in their consultation document. They considered that further consultation would be needed and therefore recommended that the Government ask the Law Commission and the Scottish Law Commission to examine the existing schemes and to make recommendations for reform. The terms of reference are at Annex A.

2.12. The Scottish Law Commission reported in September 2004<sup>1</sup>. The Law Commission are expected to report in August 2005<sup>2</sup>. This consultation is preceding the latter report so that any changes to the system for registering company charges can be made in the forthcoming Company Law Reform Bill.

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<sup>1</sup> See [www.scotlawcom.gov.uk](http://www.scotlawcom.gov.uk)

<sup>2</sup> The Report will be available on their website,

### **3. Options**

3.1 In order to assess the impact of any proposed reforms it is necessary to look at a range of options. The Government is seeking views on the cost and benefits of these. It is not formally consulting on the proposals of either Law Commission but would be happy to receive technical comments. The principal options are:

- 1 Do nothing
- 2 Implement either or both Law Commissions' recommendations
- 3 Minimum changes to improve the current scheme for England and Wales

It would be possible to implement all or some of either Commission's recommendations. If stakeholders consider that some of the recommendations should be implemented but that the costs of implementing others would not be justified by the likely benefit of doing so, they are asked to identify the particular recommendations they would not wish to see implemented and to explain why.

#### **Option 1 Do nothing**

3.1.1 Under this option the present schemes would not be changed in any way.

3.1.2 The Companies Act requires the instrument creating a charge over specified assets of a company (or a certified copy in Scotland) together with a form summarising the particulars to be delivered to the Registrar within 21 days of the creation of the charge. The Registrar then:

- checks that the particulars match the instrument
- returns the instrument to whoever filed it
- issues a certificate to the company that is legally conclusive that the charge cannot be void for want of registration or for any defect in registration,
- enters the particulars on the public record,

3.1.3 Failure to register attracts three sanctions:

- a criminal sanction that falls on the borrower;
- a civil sanction that falls on the lender: if not duly registered, the charge is void against other creditors or, in the event of the borrower's insolvency, against an administrator, liquidator; and
- a civil sanction that falls on the borrower: the sum secured is repayable on demand.

The civil sanction on lenders, known as the “sanction of invalidity”, is very effective: they normally handle the filing themselves to ensure that their charges are registered.

3.1.4. The Act also places requirements on companies who grant charges. They must keep at their registered offices:

- copies of the instruments creating registrable charges. Members of the company and its creditors have a right of inspection;
- a register of all charges, whether or not registrable. There is a public right to inspect this register.

3.1.5. The Act applies to all GB companies, but there are differences in the provisions that apply to companies incorporated in Scotland compared to those applied to other GB companies. This is because of the significant differences between English and Scots property law. The key point is that Scots law does not have an exact equivalent to the fixed charge; there is a close equivalent for land and buildings only. In practice, nearly 95 per cent of securities granted by Scottish companies are either floating charges or over land and buildings. The remainder is split between fixed charges granted under English law and charges over incorporeal moveable property.

3.1.6. In some circumstances a floating charge under Scots law is recognised under English law, and vice versa.

3.1.7 During the consultations over the last five years by the Company Law Review and the Law Commissions, hardly anyone has ever favoured this option. It would leave untouched widely-recognised problems with the current law (see paragraphs xx), and would pass over the opportunity to introduce widely-supported improvements. But it is essential that the Regulatory Impact Assessment includes the option of doing nothing, not least as a basis for comparison of the other options.

## **Option 2 Implement either or both Law Commissions’ recommendations**

3.2.1 This option comprises the implementation of the proposals for England and Wales recommended by the Law Commission and those for Scotland recommended by the Scottish Law Commission. The main part of the Scottish Law Commission’s proposals could be implemented without their proposal relating to annual returns (see paragraph 3.3.B.10).

3.2.2 The two Commissions’ proposals are different. This reflects the fact that the underlying law relating to rights in security and the law of property in the respective jurisdictions are different. The Law Commission for England and Wales was asked to consider, and recommends, a "notice filing" system under which only a "financing statement", rather than details of

the actual security transaction, would be registered. A “notice filing” system was accepted as one which could not readily be modified to accommodate the very different structures and concepts of Scots property law. Hence the different references.<sup>3</sup>

3.2.3 Where a company enters into a charge over property in both jurisdictions or over property that may be moved between jurisdictions, the different legal systems may lead to different results in terms of the validity and priority of the charge. Which system prevails is likely to depend at least partly on the location (at the time of the borrower’s insolvency) of the asset over which it is sought to enforce the charge or security.

#### **A. Recommendations of the Law Commission for England and Wales**

3.2.A.1 The Law Commission expect to make their report to Parliament in August 2005. They have provided their proposed draft Regulations in advance of their Report so that this stage of the Regulatory Impact Assessment can be complete before the introduction of the Company Law Reform Bill. The draft Regulations are at Annex C. The Commission have also provided a brief explanation of the draft regulations for use in this document. Their Report, which will be available on their website [www.lawcom.gov.uk](http://www.lawcom.gov.uk), will include a full explanation.

3.2.A.2 The main elements of the scheme that the Law Commission intend to recommend to Government for England and Wales are that:

- (i) Electronic filing will replace the current paper-based system.
- (ii) Instead of sending the charge document, only a "financing statement" will be sent. The financing statement may be brief. But it will be possible to "cut and paste" the full description of the charged assets from the charge document into the financing statement and so doing would reduce the scope for error. Registry staff will no longer check the particulars in the financing statement against the charge document. Provided that the secured party has filed a financing statement that identifies the correct company as the debtor, the charge would be validly registered in respect of the property listed in the particulars.
- (iii) The formal time-period for registering a charge will be removed. Instead, a financing statement may be filed before or at any time after the transaction (save during the ‘run-up’ to insolvency)<sup>4</sup>.
- (iv) Filing will be voluntary, in the commercial judgement of the secured party, but an unregistered charge will be ineffective as against an administrator or liquidator. The present criminal

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<sup>3</sup> DP Scot Law Com No 121, paras 1.26-1.29.

<sup>4</sup> See Insolvency Act 1986, s 245.

and civil sanctions against companies that fail to register will be removed.

- (v) The current list of charges that must be registered will be replaced by a provision that all charges are registrable unless specifically exempted.
- (vi) Charges over registered land registered at the Land Registry should not have to be registered at Companies House, but the relevant information should be forwarded by the Land Registry to Companies House. (This may depend on the introduction of e-conveyancing in England and Wales. The target date for starting this process is 2007. It is unlikely that the new scheme for company charges would be brought into effect before that date in any event.)
- (vii) Charges over financial collateral (such as securities and bank accounts) would be exempt from filing where the chargee has obtained 'control' of the collateral.
- (viii) The position of floating-charge holders will be strengthened. The priority of the charge will depend on the date of filing, unless otherwise agreed. This means that floating-charge holders will no longer have to rely on negative pledge clauses to prevent borrowers from granting subsequent fixed charges or from selling their receivables. Property subject to a floating charge will not be liable to be seized by execution creditors. This will remove the need for automatic crystallisation clauses to protect the chargee's interest.
- (ix) The position of buyers will be clarified. Briefly, buyers will take free of an unregistered charge unless they know about it. They will take subject to a registered fixed charge, unless the chargee authorised the sale. Where collateral is subject to a registered floating charge, buyers will take free of it when they buy goods in the ordinary course of the seller's business.
- (x) Companies will no longer be required to maintain a register of charges.

3.2.A.3 The Commission's proposals incorporate the modifications to the existing scheme that the Company Law Review recommended (these are set out under Option 3, below), though some of the solutions proposed are different (for example, on late registration and on charges created by overseas companies).

3.2.A.4 The Law Commission's proposals would be implemented through secondary legislation. This means that if this option were adopted there would be further opportunity to make changes to the draft Regulations.

3.2.A.5 In more detail, the Law Commission's recommendations include the following.

### Electronic notice filing

3.2.A.6A wholly electronic system for the registration of company charges will be introduced, to replace the current paper-based scheme.

3.2.A.7 To register a charge, it will be necessary only to provide brief particulars of the charge in a simple, electronic format. The original charge document would no longer be sent. Charges will appear on the register and be searchable on-line as soon as the on-line registration procedure has been completed; thus there will be no period of 'invisibility' between the date from which runs the priority of a charge and the appearance of its particulars on the register.

3.2.A.8 Formal responsibility for registration, and with it the rarely-applied criminal sanction for failure to register, will be removed from the company. It will be for the lender taking the charge to file if it wishes to protect its security.

3.2. A.9 Failure to comply with the requirement to file will render the charge ineffective against an administrator or liquidator on insolvency.

3.2.A.10 The formal 21-day time limit for registration (and thus the need for court applications for late registration) will be removed. Insolvency law relating to the run-up to insolvency will be amended to apply to charges that are registered (rather than only to charges that are created) in the relevant period.

3.2.A.11 It will be possible to file in advance of the transaction and a single filing may cover a series of similar transactions between the same parties.

3.2.A.12 The Registrar of Companies will no longer be responsible for checking the particulars that have been filed, and will no longer have to issue a conclusive certificate of registration. Provided that the secured party has filed against the correct company, the charge will be validly registered in respect of the property listed in the particulars. It will be for the secured party to ensure that the registered particulars adequately cover the property subject to the charge. A brief general description will suffice, but there will be a facility to enable the party filing to copy a full description from the charge document into the financing statement.<sup>5</sup> Registration will be proved by the electronic record, a copy of which will be sent to the secured party.

3.2.A.13 The company will be empowered to have inaccurate registrations corrected or removed quickly and simply.

3.2.A.14 The current list of charges that must be registered will be replaced by a provision that any charge is registrable unless specifically exempted.

3.2.A.15 Charges over personal property for which there is a 'specialist register' (ships, aircraft and some intellectual property) will be registrable for

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<sup>5</sup> This would mean that reading a search result could take longer where there are lengthy particulars; but there correspondingly there would be less need to ask the debtor or the chargee for further details.

validity purposes under the scheme, and there will be clear rules to determine priority conflicts over such assets.<sup>6</sup>

3.2.A.16 Provided that the Land Registry's proposals for electronic conveyancing go ahead as anticipated, the scheme will not require Companies House registration of charges over registered land that have been registered at the Land Registry; the information on the Land Registry will be forwarded to Companies House for information purposes. Charges registered at the Land Register will be effective in insolvency and their priority will depend on rules of land law.

#### Priority

3.2.A.17 Priority between competing charges will be by date of filing, unless otherwise agreed between the parties involved. This rule will apply whether the charge is fixed or floating, and will simplify the current law.<sup>7</sup>

3.2.A.18 The scheme will also provide that property subject to a floating charge will not be available to execution creditors. This will make it unnecessary to use automatic crystallisation clauses, which are uncertain in their operation and potentially risky to the chargee.

3.2.A.19 The effect of registration on the rights of a person who buys the property without knowing of the charge will be clarified. An unregistered fixed charge will not affect a buyer without actual knowledge of it; a registered fixed charge will be binding on the buyer. If the charge is floating, the existing law that a buyer in the ordinary course of business will take free will be unchanged.

#### Charges created by companies incorporated outside England and Wales

3.2.A.20 Charges created by an overseas company over its assets in England and Wales (including intangible assets that in private international law are treated as 'situated' in England and Wales) will have to be registered to be effective like those of a company registered in England and Wales. If property already subject to a charge is brought into England and Wales, the charge will not need to be registered for 60 days. (There will be an exception for aircraft and ships that are registered abroad.)

3.2.A.21 A Scottish company wishing to create a charge over assets in England in accordance with English law would be required to file a financing statement in the same way as English or overseas companies.

#### Financial collateral

3.2.A.22 The scheme will include provisions dealing with financial collateral (financial instruments and 'cash' within the meaning of the

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<sup>6</sup> Consultation indicated that the cost of double registration in both the specialist register and at Companies House was generally thought worthwhile, for the benefit of finding information at one source.

<sup>7</sup> Under current law, chargees use negative pledge clauses to attempt to alter the 'default' priority position for a floating charge that enables a chargor to grant subsequent fixed charges that will rank ahead of the floating charge. However, such clauses are not always effective against subsequent chargees. Dating priority from time of registration will make it unnecessary for a chargee to rely on a negative pledge clause in order to prevent subsequent charges gaining priority.

Financial Collateral Arrangements Regulations 2003 (in which ‘cash’ means money held in an account and certain other debts), and also other financial assets held through intermediaries.). These will address the particular needs of the financial markets, clarifying as far as possible uncertainties left by the Financial Collateral Directive and the implementing Regulations:

- A chargee who has obtained ‘control’ of the financial collateral will not have to register the charge;
- There will be clear rules on the priority of competing charges perfected by control; and
- There will be rules on purchasers of investment property, designed to ensure that it remains freely transferable in line with the aims of the Financial Collateral Directive.

### Receivables financing

3.2.A.23 It is also proposed that sales of receivables of the kinds that are commonly factored or discounted should be registered in the same way as charges.

3.2.A.24 The priority of competing charges and sales of receivables should be governed by the date of filing, in place of the current rules which are practically unsuited to the needs of modern receivables financing.

3.2.A.26 Clauses in the contract generating the receivable that purport to prohibit or restrict the assignment of the receivable would be of no effect against an assignee.

## **B. Recommendations of the Scottish Law Commission**

3.2.B.1 The Scottish Commission’s principal suggestions for reform are described in paragraph 1.20 of their report<sup>8</sup> as being, in broad outline:

### Floating charges

3.2.B.2 Registration in a register of floating charges should be essential in order to constitute a floating charge. Thus, without registration no inchoate security capable of later crystallisation is created. Floating charges should, in principle, rank inter se and with other forms of security by date of registration or constitution of the real right as the case may be.

3.2.B.3 Any variation, assignment or discharge of a floating charge requires to be registered before it may affect any third party.

3.2.B.4 To facilitate the mechanics of a secured transaction it should be possible to register an advance notice, the floating charge, if registered within 21 days, being deemed to have been registered on the date of registration of the advance notice.

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<sup>8</sup> Report on Registration of Rights in Security by Companies, Scot Law Com No.197 Scottish Law Commission

### Other rights in security

3.2.B.5 All forms of security other than floating charges may be granted by non-corporate debtors and in Scotland the constitution of an effective right in security is dependent on some form of publicity. It is considered that there is no sufficient reason for submitting the validity of such security rights to any additional registration requirements because the grantor is a company. The present requirement to register particulars of certain of these security rights with the Registrar of Companies should cease.

### The company's own register: annual returns

3.2.B.6 The current statutory requirement to maintain, at the company's registered office, an internal register of all securities specifically affecting property of the company and all floating charges should be removed. Instead:

- (i) the annual return submitted by the company to the Registrar of Companies should include certain short details of all rights in security granted by the company but not discharged at the return date; and
- (ii) a company should be under a statutory duty to supply to anyone making the request, and paying such fee as may be charged within prescribed limits, the same details respecting any right in security granted after the last return date; and
- (iii) inspection of copies of the security documents at the company's registered office should be allowed, again on payment of such fee as may be charged within prescribed limits.

3.2.B.7 The complete list of their Recommendations is at Annex C.1 and their Draft Legislative provisions at Annex C.2.

3.3.B.8 The proposed Register of Floating Charges would take the form of an electronic database and it is envisaged that it would be maintained by the Registers of Scotland.

### Partial implementation of the Scottish Law Commission's proposals

3.2.B.9 The Scottish Law Commission's proposals regarding floating charges in Scotland and the cessation of any requirement to register particulars of security rights with the registrar of companies are not dependent on implementation of the suggestion that brief details of extant securities be included in the annual return. That suggestion, and the ancillary optional proposal regarding the provision of updating information, were offered as a means of assisting financial transparency by complementing the financial information contained in the annual accounts, were that thought desirable. The Scottish Law Commission's proposals therefore have within them the option of:

- simply implementing the reforms on the Scottish law of floating charges and

- the cessation of registration of particulars at Companies House,

without implementing the suggestion regarding the annual return.

3.2.B.10 Although not proposed by the Scottish Law Commission, it would be possible for Registers of Scotland either to provide brief particulars of companies' floating charges to Companies House – as is proposed for England and Wales (see paragraph 3.3.A.16) – or for there to be electronic links between these two Registers. Similarly, it would be possible for the brief particulars of companies' standard securities to be copied to Companies House. This information-sharing might be an alternative to the Scottish Law Commission's suggestion regarding the annual return.

### **Option 3: Improve current scheme for England and Wales**

3.3.1 Provided the Scottish Law Commission's proposals for floating charges and of other rights in security are adopted, there would be the option for England and Wales of improving the current scheme in accordance with the provisional recommendations of the Company Law Review. The Company Law Review consulted over a set of proposals for improvements to the present system for registration of company charges. In the light of the responses, in particular the criticisms of the present system and the support for notice-filing, and noting that more fundamental changes were outside their remit, the Company Law Review recommended that the Law Commissions be requested to examine the system for registering company charges and security and "quasi-security" generally over property other than land. However they did reach provisional conclusions, including recommendations for improvements to the existing system if it were decided not to introduce notice-filing. Under this option, there would be no change to what is achieved by filing (ie no change the law relating to priority).

3.3.2 These recommendations were intended to deal with what were considered to be the most serious problems. From the views that have been expressed to us or that have been reported to us by the Law Commission, there is strong support for tackling these problems in the ways suggested by the Company Law Review, or at least a recognition that they will probably have to be tackled along similar lines. There also appears to be wide-spread support for a few changes that were not included in the Company Law Review's 'improvements to the current system', in particular the introduction of a scheme that would allow registration using electronic documents in place of paper. The Company Law Review's 'improvements to the current system' and the further changes just referred to seem to us to represent a 'minimum package' that could be introduced if the full scheme for England and Wales recommended by the Law Commission were not to be introduced.

3.3.3 The registration scheme recommended by the Law Commission for England and Wales cover all the points in this minimum package, though sometimes the solutions recommended differ. (For

example, The Law Commission recommends different solutions for late registration and for charges created by oversea companies. The Law Commission's proposals are noted as each item in the 'minimum package' is examined below.) Thus adoption of the minimum scheme would amount to partial implementation of the Law Commission's recommendations. It can be described equally accurately either as 'a partially new scheme' or as 'improvements to the current system'.

3.3.4 The main modifications to the existing schemes that the Company Law Review recommended were:

- (ii) to abolish the requirement for the charge instrument or a certified copy to accompany the form registering the charge;
- (iii) to make the lender liable for inaccuracies in information filed;
- (iv) to make the registrar's certificate conclusive only as to the date and time of registration;
- (v) to make registrable charges over all forms of obligations except those specified;
- (vi) to establish arrangements so that a single filing achieves registration at both the Land Registry and Companies House.
- (vii) that a charge be valid for, and only for, the property or classes of property included in the filed particulars;
- (viii) to abolish the requirement for a court order for late registration of a charge;
- (ix) in the event of failure to register a charge, abolition of:
  - a) the criminal sanction on the company, and
  - b) the civil sanction that the sum secured is payable on demand;
- (x) that corporate members of Lloyds not be required to register separately each charge entered into under trust arrangements;
- (xi) to abolish the requirement for companies to maintain their own registers of charges;
- (xii) to abolish the requirement for Companies House to maintain a separate register of charges for each company.
- (xiii) to rationalise the scheme's application to oversea companies.

The further change that seems to be almost universally supported would be

- (xiv) to enable registration to be carried out via electronic documents.

Charge Instrument (or certificated copy) to accompany registration of charge; Liability for inaccuracies in information filed

3.3.5 It is convenient to treat these two recommendations together. Under the present system, the instrument creating the charge is sent to the Registrar together with a form summarising the particulars within 21 days of the creation of the charge. This may be done by either the lender or the borrower; in practice, it is almost always the lender as it is he that suffers most if the charge is not filed in time. The Registrar then checks that the form has been completed, enters the particulars in the register, and returns the instrument to the presenter. The Registrar also provides a certificate which is conclusive evidence that the Companies Act requirements for the registration of company charges have been satisfied<sup>9</sup>. This means that the charge is valid even if the particulars are inaccurate, and even if the certificate were issued in reliance on a court order which was subsequently overruled on appeal. There is no similar requirement for the filing of any other document.

3.3.6 The Company Law Review recommended that the schemes could be simplified by dispensing entirely with the delivery of the document creating the charge. Instead, the requirement might be for the company only to submit the particulars of the charge, which would include the date of its creation. In this case, Companies House would check only that the required particulars had indeed been filed within 21 days of the declared date of creation.

3.3.7 Under this option, Companies House would be able to handle the information relating to company charges in the same way as it handles other company information that it has to place on the public record. And, as recommended by the Company Law Review, any civil liability arising from errors in filed particulars will lie with the lender. This proposal would be supported by the provision in the Company Law Reform Bill making it an offence knowingly and recklessly to file misleading information.

3.3.8 In substance the effect of this change would be almost identical to the Law Commission's recommendation that a charge should be registered by filing of a financing statement containing particulars of the parties and the charge (including a description of the collateral, which could be brief or as full as the parties wish). In practice the only information that would be submitted under the Company Law Review's proposal but not under the Law Commission's are

- (a) the date of creation of the charge (because under the Law Commission's proposal the filing may be made in advance) and
- (b) the amount secured (which is often considered to be redundant since the figure shown is unlikely to remain accurate.)

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<sup>9</sup> Section 401(2)(b) for England; section 418(2)(c) for Scotland

As now, under either scheme it would then be up to the searcher wanting more information to ascertain the details of the charge from the company.

### The Registrar's Certificate

3.3.9 The Company Law Review recommended that, whatever the system of registration of charges, the conclusive certificate should be abolished and that entry on the register at Companies House should be conclusive evidence of the date of registration.

3.3.10 Under the Law Commission's recommendations the Registrar would not issue any form of certificate (as we saw earlier, there would be no requirement to register within 21 days.) Proof that a financing statement covering the charge was registered at a particular time would be provided by production of either a 'verification statement' which would be sent to the party filing immediately after registration of the financing statement, or of a search result, which would show the date and time at which each financing statement was registered.

### Charges over land

3.3.11 Charges over land in England and Wales are registrable at Companies House. In addition, most such charges are registrable at the Land Registry which ensures both the validity of the charge and its priority over subsequently-created charge. (In the case of equitable charges, their entry in the Land Register does not guarantee their validity.) In Scotland, standard securities are registrable both with Registers of Scotland and at Companies House.

3.3.12 Responses to consultations have shown that the dual registration requirement serves a purpose: the information is put on the public record relating to the company and is therefore easily found (even if the company changes its name). With regard to land, this benefit could be achieved by the Land Registry sharing information with Companies House, provided there were a statutory obligation on Companies House to place the information on the public record. This would meet the Company Law Review recommendation of arrangements so that a single filing achieves registration with both Companies House and the appropriate specialist register be pursued. Indeed their recommendation on the Registrar's certificate would only be practicable if this change were also made.

3.3.13 The Law Commission's recommendations on registration of charges over registered land are to the same effect. Charges over registered land that are registered at the Land Registry would not need to be registered on the company security register. Information about them would be forwarded by the Land Registry and would be available to searchers of the company security register. The details shown could if necessary be adjusted (by way of an additional statement) to reflect subsequent alterations in relation to the land charge. Other charges over land would have to be registered on the company security register.

3.3.14 This proposal may depend on the introduction of e-conveyancing in England and Wales. Any reforms to the registration of company charges are unlikely to be brought into effect before then.

#### Registrable charges

3.3.15 The Company Law Review considered the best approach would be to make registrable charges over all forms of obligations (whether or not financial and whether present or future) excepting only those specified. This is the approach also recommended by the Law Commission.

#### 'Late' registration

3.3.16 If a charge is not registered with 21 days of its creation, then either the company or the chargee may apply to the court for an order extending the period for its registration. Normally, provided that the company is not being wound up, the court will allow registration on terms that do not prejudice rights of unsecured creditors acquired between the date of the charge's creation and its registration.

3.3.17 If a charge is not registered within 21 days of its creation (and in the absence of a court order), it is void against a creditor or an administrator or liquidator: this is called the "sanction of invalidity". In addition, if the charge is not duly registered, there is a criminal sanction on the company and the sum secured is payable on demand.

3.3.18 The Company Law Review recommended that:

- Late registration be possible without application to the court provided that at the time of registration, no winding-up petition has been presented and no meeting has been convened to pass a resolution for a creditors' voluntary winding-up petition; and
- In the event of late registration, the charge should be treated from then on as it were registered within time, save that it should rank behind any prior registered charges.
- Abolition of the civil sanction that the sum secured is payable on demand if the charge is not duly registered; and
- Abolition of the criminal sanction.

3.3.19 The problem with this Company Law Review recommendation is that Companies House would not know whether the date stated as the date of creation of the charge was accurate, nor whether a late registration should be refused because the conditions have not been met. This could be resolved by making the late registration invalid if the conditions were not met, but that might leave a lender who had an arguable case for being permitted to register late not knowing whether or not the registration would be treated as valid if and when the question arose.

3.3.20 The Law Commission's recommendations are that registration should be effective if it is made at any time before the debtor company's

insolvency, subject to amending Insolvency Act 1986 s 245 to cover floating charges that are only registered during the run-up to the insolvency. As priority of charges would depend on the date of the relevant filing, this would seem to have almost identical effects to the Company Law Review's recommendations. There would be no need, however, for a special administrative process to deal with late registration, nor any risk that a 'late' registration might subsequently be held ineffective on the grounds that the conditions for late registration had not been met.

#### Defective Particulars

3.3.21 A court order is also required to remedy any omission or misstatement of any particular in a charge of memorandum of satisfaction. The Company Law Review considered that defective particulars should not invalidate the charge as a whole but that a charge should only be valid for the property or classes of property properly included in the filed particulars. Where the particulars are inaccurate by the wrongful inclusion of an asset, they considered it should still be valid for the assets rightly included but that it should be possible, without a court order, to cancel the filing insofar as it applies to assets not subject to the charge.

3.3.22 It would be consistent with the Company Law Review, although not explicitly recommended by them, to abolish also the requirement for a court order to rectify any other errors.

3.3.23 The Law Commission's recommendations are almost identical in effect, though again not requiring a special administrative procedure. Once a financing statement has been registered identifying the correct company as the debtor, a charge covered by the financing statement would be registered and effective in respect to collateral described on the financing statement (provided of course that it was indeed within the charge agreement). It would not be effective with respect to collateral that was omitted from the financing statement. The omitted collateral could be added later by means of an additional statement, but the priority of the charge in respect of the collateral in question would be from when the additional statement was registered.

#### Corporate members of Lloyds

3.3.24 The current registration requirements create particular problems and high compliance costs for the corporate underwriting members of the Lloyd's insurance market. This burden is particularly acute in relation to the trust arrangements supporting certain categories of insurance business which are structured, in accordance with the requirements of foreign insurance regulators, on a standard form basis by reference to individual syndicates within the Lloyd's market. For such business, corporate members of Lloyds are currently obliged to make standard form filings annually in respect of each syndicate on which they participate for each category of such business.

3.3.25 The Company Law Review recommended that the filing requirement for each category of insurance business for corporate members

of Lloyds should be to send a single set of particulars of the relevant standard form trust deed together with a list of the syndicates on which the company underwrites that category of business.

3.3.26 Under the Law Commission's recommendations most of this category of charge would not need to be registered at all, since absence of publicity about it is unlikely to mislead anyone. Only the deposit trust deed or security and trust deed granted by every member would be registrable.

#### Companies own registers of charges

3.3.27 At present, companies are required to keep a register of all charges over their property, whether or not the charge is registrable at Companies House. This is in addition of the requirement for them to keep at their Registered Offices copies of the instruments creating registrable charges. The Company Law Review recommended abolition of the statutory requirement for companies to maintain registers of their charges. The Law Commission's recommendation is the same.

#### Registers maintained by Companies House

3.3.28 Companies House registers and maintains information about charges in two formats. First it places all the prescribed forms relating to charges on the company's public record. It also extracts relevant information from each form and make it available in information provided electronically. Second, for each company it maintains a register of charges, usually called the company's "mortgage register", which record the receipt of the forms relating to charges with very brief details of their content. They also record the appointment and removal of receivers. These statutory mortgage registers add nothing to the totality of the information already available on the company's public record. But their maintenance is a statutory obligation placed on the Registrar. The Company Law Review recommended that this statutory obligation be abolished.

3.3.29 Under the Law Commission's proposals the form of the company security register would be at the Registrar's discretion, provided that the register is adequately searchable. There would be no need for a 'separate' register, even if such a concept is meaningful when all records will be electronic and can be linked to one another.

#### Oversea companies

3.3.30 Ideally every company would register its charges in its own country of jurisdiction. However, many overseas jurisdictions have complex and restrictive systems for creating charges. In some, fixed charges may be created over only certain types of property, and many do not recognise floating or 'enterprise' charges. Further, not all jurisdictions have central registers for company charges, and those that do usually require registration only of the types of charge recognised in the jurisdiction. Requiring oversea companies to register their charges over GB assets is therefore needed to protect potential purchasers of these assets and to provide information to others dealing with the company.

3.3.31 At present, charges over assets located in GB granted by overseas companies with a GB place of business are registrable. There are problems with the present requirements:

- the requirement to register applies whether or not the company has in fact registered itself at Companies House as having a GB place of business: so the lender may not be certain whether or not the charge is registrable.
- the law makes no mention of charges over assets located overseas when the charge was created but subsequently brought into GB. This results in a nonsense: the charge cannot be registered within the time limit but is void for not having been registered in time.

Following a 1980 court case, a work-round has been devised: Companies House keeps a special file<sup>10</sup> for the charges of those overseas companies that do not have a GB registered branch or place of business.

3.3.32 The Company Law Review recommended that charges over GB assets granted by an overseas company that had registered a branch or place of business in:

- England and Wales, be subject to the same registration requirements as would apply to a company incorporated in England or Wales;
- In Scotland, be subject to the same registration requirements as would apply to a company incorporated in Scotland.

The Law Commission has considered this option but recommends that charges created by any overseas company over its property in England and Wales should be subject to the same scheme as charges created by English companies, so that both the registration requirement and the rules that the Law Commission recommends should govern priority will apply to all charges over company assets in England and Wales. Charges over goods brought into the jurisdiction (other than aircraft or ships registered abroad) would have to be registered after 60 days.

#### Electronic registration (or 'filing')

3.3.33 There appears to be almost universal support for moving to an electronic system of registration for company charges. Some of those who have expressed support for this seem to have in mind merely that the charge document and Form 395 could be sent to Companies House in electronic form. However when electronic registration is coupled with the other minimum changes outlined above, it is evident that the registration should involve the submission to the Registrar, by electronic means, of only short particulars of the charge; and that these would be recorded without being checked by Registry staff.

3.3.34 The scheme would provide for registration of existing charges, rather than for "notice" or "advance filing" as recommended by the Law

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<sup>10</sup> The Slavenburg Register

Commission (see Option 2). It might however allow for the filing of a priority notice, rather as is permitted in the Land Registry and as the Scottish Law Commission recommended for floating charges (see paragraph 3.3.B.1(iii)).

### Scotland

3.3.35 Improving the current scheme is an option for England and Wales only. If applied to Scotland, it would not implement even in part the reforms proposed by the Scottish Law Commission. In particular it would continue the requirement to effect some form of filing for fixed securities, even though registration at Companies House is not necessary, since they received some form of publicity for their constitution. Nor would it effect the improvements to the law of floating charges in Scotland. But more importantly, filing a financing statement or "notice-filing" is not a system which can readily be adapted to or accommodated within the very different principles and structures of Scots law.

3.3.36 If it were decided to improve the current scheme for England and Wales, the key elements of the proposals of the Scottish Law Commission would be implemented, ie:

- (i) the creation of a new specialist register of floating charges with registration effecting creation of the floating charge under Scots law;
- (ii) no requirement for registration at Companies House of any security granted by a Scottish company, or of a charge created by an overseas company over property in Scotland. The existing registration requirements, with the 'minimum changes' proposed under Option 3, would be retained for charges granted by English and overseas companies over their property in England;
- (iii) abolition of the requirement for GB companies to maintain their own registers of charges.,

It would also be possible, but not essential, to implement the proposal:

- (iv) companies incorporated in Scotland would be required to include the details of all outstanding charges in their Annual Return, and to provide anyone who so requests with details of any charge granted since the last Annual Return.

## **4. Costs and Benefits**

### **Sectors and groups affected**

4.1.1 The proposals would affect:

- All GB companies that borrow or wish to borrow against the security of any assets

- Those who lend to GB companies against the security of their assets and those who lend to overseas companies against the security of their GB assets;
- Factors, discounters and other purchasers of receivables;
- All creditors of GB companies and of overseas companies with GB assets;
- Credit reference agencies and others who need information on the financial position of the company;
- Anyone who buys an asset that might have been used as security for borrowing by a company.

4.1.2 A study of financing arrangements for smaller quoted companies, by the Bank of England in 2004,<sup>11</sup> concluded that banks tend to favour security, especially on longer term loans, to smaller quoted companies although the firms themselves had an aversion to secured finance. In the survey, only 18% of those companies that borrowed did so on an unsecured basis. On aggregate the survey found that some 59% of borrowers provided a fixed charge on debt facilities and 48% provided a floating charge. An earlier study by Franks and Sussman<sup>12</sup> examined the financing arrangements between three major clearing banks and small and medium sized companies. They found that 80-95% of debt was covered by floating charges and 55-90% was covered by fixed charges

4.1.3 We request stakeholders' views on these figures and would welcome any more recent evidence that shows the relative extent of secured and unsecured borrowing by GB companies.

## **Benefits**

4.2 We welcome stakeholders' views on the benefits of the different options. Where possible, an estimate is given; we would also welcome comments on and corrections to these estimates. However many of the benefits are difficult to quantify, particularly those relating to reduction in uncertainty.

### **Option 1 Do nothing**

4.3.1 The main advantage of retaining the current schemes would be continuity: the schemes, which are based on that introduced in England and Wales in 1900, have been in place, unchanged, for 20 years. There are two main benefits of these schemes.

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<sup>11</sup> Brierley, P and Young, M., 'The Financing of smaller quoted companies: a survey', Bank of England, Quarterly Bulletin, Summer 2004, pp.160-169.

<sup>12</sup> Franks, J and Sussman, O., 'The Cycle of Corporate Distress, Rescue and Dissolution. A Study of Small and Medium Size UK Companies', April 2000.

- They ensure public information about a wide range of a company's securities being available at the same place as its other public information, ie at Companies House. This benefits all those interested in the financial strength of individual companies, not just those whose lending is secured.
- They provide protection for the rights of secured parties in the event of a company's insolvency by giving publicity to security arrangements which under English law might otherwise be concealed: a direct benefit to secured parties and an indirect benefit to companies whose borrowing is thus facilitated.

In addition, the existing schemes have very similar arrangements for the registration of charges in both jurisdictions.

## **Option 2      Implement either or both Law Commissions' recommendations**

### **A.                Recommendations of the Law Commission for England and Wales**

4.3.2.A.1      Implementation of the recommendations of the Law Commission would bring all the benefits from modifying the existing scheme and, in addition, widespread benefits from the improvements in the clarity and accessibility of English law on priority of competing interests, including competing interests over financial collateral. There would also be particular advantages to various groups affected.

4.3.2.A.2      The advantages to English companies would be that:

- they would no longer be legally responsible for registering charges: filing would be up to the secured party;
- the lower costs of the scheme to the lender, and its greater certainty and reliability, should make it easier to obtain secured credit and reduce its cost;
- It will be easier to obtain receivables financing because anti-assignment clauses will no longer be effective against the assignee.

4.3. 2.A.3      The advantages to the secured lender to English companies who uses the current registration system would be:

- filing would be simple, using only readily available information, and not requiring legal expertise. There would be no need to prepare special documentation for sending to the registry, or to send the charge document.
- there would be no fixed time limit on filing and no need for court proceedings for 'late' registration;

- the filing could be made, provided the other party agrees, before the security agreement is finalised; and one filing could cover a series of future transactions;
- charges will appear on the register as soon as the registration of a financing statement has been completed, which will be within a few minutes of a properly completed statement being submitted. Periods of “invisibility” would be largely eliminated;
- the rules of priority would be clearer and suited to modern financing methods. Once the secured party had filed, it could be confident that its security would have priority, as against any other secured party, as from the date of filing, save in those specific cases in which the scheme provides otherwise. The same would apply as against someone who has bought the assets charged from the company

In the year to 31 March 2005, nearly 200,000 charges were registered at Companies House in Cardiff. Of these, nearly 2,000 were rejected for being out of time of which about a third required court orders. It is likely that the fee for electronic registration would be less than that currently charged, £13. However the fee is probably a small element of the total cost of preparing particulars and delivering them and the charge instrument to Companies House. The saving from electronic registration is likely to be at least £50 per charge, ie about £1million per annum. The saving from the abolition of a fixed time limit for filing would probably be over £1 million, arising from £1,000 for a court order and lower costs for the other late charges. Reliable statistics are not available on charges registered at both the Land Registry and Companies House. Given the expected saving from electronic registration, the additional saving from ending the requirement for double registration is unlikely to be more than £0.2million.

4.3. 2.A.4 The advantage, whether directly or through credit-reference agencies, to the customers and suppliers of companies and all their actual and potential creditors would be, as now:

- fast and cheap searching
- at the same place as other statutorily required public information about a company

for information on the existence of:

- floating charges, fixed charges over all assets (other than those explicitly excluded) and of charges over land granted by any company incorporated in England and Wales;
- charges over assets in GB granted by any overseas company;
- charges granted by any company incorporated in Scotland over assets in England and Wales.

4.3. 2.A.5 The advantages to those who take security over financial collateral of English companies would be:

- a reduction in the uncertainty surrounding the notion of ‘control’ in a way that will encourage good commercial practice;
- clear rules of priority over financial collateral.

It is difficult to quantify this benefit. However a court case arising from a dispute over either the meaning of “control” or priority over financial collateral would involve considerable costs; avoidance tactics are likely to be an ongoing cost for all those involved.

4.3.2.A.6 The advantages to receivables financiers would be two-fold. First, though they would have to file when they buy or take a charge over a company’s receivables, they will have a ready way of discovering any existing charge or sale of the receivables that has been filed, and can safely ignore any that has not. Once they have filed, they will ensure their own priority, without having to notify account debtors who owe the receivables. Secondly, they would no longer be affected by terms in the contract creating the receivable that prohibit or restrict assignment.

4.3.2.A.7 The advantages to buyers of goods from a company would be:

- they will not be affected by an unregistered charge unless they know of its existence;
- it will be clear when they will be bound by filed security interests, and so should search the register, and when not;

4.3.2.A.8 The advantages to liquidators and administrators would be the greater ease in determining who has an effective security interest over what assets.

4.3.2.A.9 The advantages for Companies House would be their no longer having to check particulars of charge documents; the register will show the information as supplied by the secured party.

4.2.3.A.10 The advantages for the Land Registry would be the removal of the need to register company charges separately at Companies House, which is an obstacle to the development of e-conveyancing

## **B. Recommendations of the Scottish Law Commission**

4.3.2.B.1 Implementation of the recommendations of the Scottish Law Commission would tailor the law relating to company security interests to Scots property law. Under Scots law, it is not possible to create real rights without publicity, eg by registration or possession. This means that a company cannot conceal its encumbrances, irrespective of whether charges have to be registered at Companies House.

4.3.2.B.2 The Scottish Law Commission’s proposals would mean that security rights constituted in the normal way would no longer be subject to an additional registration requirement just because the grantor is a company. The proposals thus have the benefit of getting rid of an unnecessary requirement for the validity of such rights. Since, in Scotland,

most securities, other than floating charges, are standard securities over land removal of the requirement to register particulars at Companies House will be of particular benefit to conveyancers and should result in the saving of time and expense and the avoidance of the practical difficulty presented by the current requirement to register within 21 days.

4.3.2.B.3 The recommendations for floating charges have among others the benefit of removing a structural deficiency in the current law. The default rules on ranking will accord with what currently has to be achieved by the almost invariable use of a negative pledge clause. Registration of the text of a floating charge will avoid error in the preparation of particulars and the need for registry staff to check such particulars. The proposed register will be an electronic one enabling electronic searching in due course and a floating charge to be registered electronically. Introduction of advance notices for floating charges will assist the mechanics of settling secured transactions. The proposal for a single register of floating charges also rationalises the arrangements for giving publicity to floating charges created under Scots law by industrial and provident societies, European economic interests groupings, limited liability partnerships and oversea companies.

4.3.2.B.4 In the last financial year, some 17,000 charges were registered at Companies House in Edinburgh, of which almost all were either standard securities over land or floating charges. However it is unlikely that the saving directly from the recommendations would exceed £0.5million.

4.3.2.B.5 If the recommendations regarding the inclusion of information on securities in the annual return were implemented, those wishing to know about a particular Scottish company's encumbrances should be able to obtain:

- from the public record at Companies House, brief particulars of securities in force at the time of the company's last Annual Return.
- from the company itself, for a prescribed fee, brief particulars about those securities granted subsequently.
- In addition, full information about a company's floating charges would be available from the proposed new Register of Floating Charges.

The information would also be available from the public record at Companies House under the alternative suggestion of Registers of Scotland providing Companies House with brief particulars of companies' floating charges and standard securities (see paragraph 3.3.B.10).

### **Option 3 Improve the existing scheme for England and Wales**

4.3.3.1 Modifying the existing scheme would retain the benefits of the existing scheme (see paragraph 4.3.1). In addition, both those taking security from companies for their lending, ie lenders, and the companies themselves would benefit from a reduction in the operating costs of the scheme from:

- electronic filing; and
- the operational savings for Companies House.

There would be benefits for lenders from:

- abolition of the requirement to deliver the charge document;
- ending the requirement for charges over land to be registered at both a Land Registry and Companies House;
- abolition of the need for a court order for late registration;
- rationalising the scheme's application to overseas companies so it is immediately clear whether or not a charge is registrable

All companies that take secured loans would benefit from:

- the abolition of sanctions on them in the event that the charge is not registered; and
- no longer having to maintain their own registers of charges. (We understand that compliance with this requirement is low, therefore its removal would only bring a notional benefit.)

Corporate members of Lloyds would benefit from the reduction in registration requirements.

It will be seen that, compared to Option 2, Option 3 would not bring the benefits of clarified and modernised rules of priority as between secured parties or as between a secured party and a person who has bought the asset; the strengthening of the floating charge; the additional information about charges created by overseas companies that do not have a registered branch or place of business. There would be no reduction of the uncertainty surrounding charges over financial collateral and there would be no advantages to receivables financing.

Option 3 might not wholly solve the issues surrounding late registration.

### **Compliance costs**

4.4 We welcome consultees' views on the costs of the different options. Where possible, an estimate is given; we would also welcome comments on and corrections to these estimates. However many of the costs are difficult to quantify, particularly those relating to reduction in uncertainty.

## Option 1 Do nothing

4.4.1.1 The main problem with the present scheme is **uncertainty**. In addition, the present system has the following costs and problems:

- (a) The date of **creation** of the charge is critical in determining both the validity and the priority of the charge. But it is not always immediately apparent. In some cases, the date may be contingent; while in Scotland, other than for a floating charge, it is the date of creation of the real right, by for example, registration in the land or other specialist register.
- (b) During the 21 days after its creation, the charge is valid with its priority determined by its date of creation, but it is not visible to anyone inspecting the register at Companies House. This is referred to as the “**invisibility**” problem; it may be greater in theory than practice, as lenders can withhold funds until any previously created charge is either registered or out-of-time
- (c) The 21 days for filing is a tight window; late filing requires an application to court. Companies House report nearly 40 a week miss the deadline. In practice, many charges are reconstituted (as a cheaper option than a court order to ensure filing is in time, though this risks a loss of priority.
- (d) The position in English law as regards **priority** of competing claims is complicated and the law incomplete. Relevant factors may include the type of assets; the date of creation; whether the charge was registrable and if so whether it was registered timeously; whether the competing interests are legal or equitable; and, in some cases, whether a subsequent secured party had notice of a negative pledge clause.
- (e) The Registrar has to issue a certificate that is **conclusive** evidence that the registration requirements have been satisfied.
- (f) The requirement to present the actual charge instrument (for Scottish companies, a certified copy) to Companies House and for Companies House then to return it to the presenter imposes costs.
- (g) The categories of registrable charge are not wholly in line with current practice. For Scotland, the list does not include either all the assets over which security may be granted nor all forms of security. Some standard forms of charge used under English law are not registrable. Therefore the information at Companies House is a partial picture of the extent of encumbrances. incoherent.

- (h) Fixed charges over assets for which there is a specialist register have to be registered in two places (ie Companies House and the special register).
- (i) For floating charges under English law, charge documents have to make special provision (eg “negative pledge clauses” and “automatic crystallisation clauses”) to ensure that the floating charges are effective.
- (j) The position under English law of a person who, unknowingly, buys property that is the subject of a security is unclear.
- (k) For English and Welsh companies, the detail of the information at Companies House quickly becomes out-of-date: it is no more than a record of whether or not there is a registrable charge over a particular asset. Nor can the particulars at Companies House be treated as wholly reliable for Scottish companies.
- (l) The sanctions on the borrower for failing to register a charge are inappropriate and unnecessary.
- (m) Compliance with the requirements for companies to hold and to reveal information is poor.
- (n) The system for registering charges does not fit easily with property law in Scotland. Though broadly similar, there are differences in the current rules on registration at Companies House vary as between England & Wales and Scotland. For example, there is a requirement in Scotland, but not in England, to register instruments of alteration and memoranda of satisfaction for floating charges.
- (o) The scheme is particularly onerous in its application to underwriting by Lloyds.
- (p) The scheme is flawed in its application to charges over GB property granted by oversea companies.
- (q) The scheme applies to registered companies only, ie it does not apply to other forms of GB companies such as Industrial and Provident Societies, Building Societies, or companies formed under Royal Charter, or a private Act or Parliament, or to other business entities, such as partnerships or sole traders.
- (r) The need to register company charges affecting registered land at Companies House as well as at the Land Registry is an obstacle to the development of e-conveyancing. In Scotland, the current registration requirements present an obstacle to including company standard securities in the automated registration of title to land system.

The total annual cost of Companies House operating the current paper-based a paper system is nearly £0.5million.

**Option 2      Implement either or both Law Commissions' recommendations**

**A.                Recommendations of the Law Commission for England and Wales**

4.4.2.A.1      The Law Commission's proposals are expected to reduce substantially the ongoing costs for registering companies' charges. The main costs associated with their Commission's recommendations would be:

- the transitional costs for lenders in adapting their systems and training their staff.
- the costs of setting up the new system at Companies House.

**B.                Recommendations of the Scottish Law Commission**

4.4.2.B.1      The main costs associated with the Scottish Commission's recommendations would be the one-off costs associated with establishing a Register of Floating Charges.

4.4.2.B.2      If the recommendations relating to the Annual Return were also implemented, there would be costs:

- for Scottish companies of
  - providing information about their outstanding encumbrances with their Annual Returns. Since the Registrar of Companies operates a "shuttle return", in the case of a company whose secured financing arrangements had not changed, or not changed significantly during the year, the cost would minimal;
  - providing, on payment of the prescribed fee, information about securities to any person who so requests. The fee should cover the cost to the company.
- For creditors and potential creditors, from
  - the loss of up-to-date information at Companies House about Scottish companies' encumbrances and having to obtain it from the company instead;

- possible omissions and inaccuracies in the record at Companies House relating to Scottish companies' encumbrances, noting that, as information in the annual return is not linked to the validity of the charge, it may be less accurate than information under the present system or that under the English Law Commission's proposed scheme

## **C. Cross-jurisdictional**

4.4.2.C.1 Implementation of either Law Commission's proposals will remove the current "reciprocity" in registration requirements whereby companies incorporated in Scotland register only in Edinburgh and those incorporated in England and Wales register only in Cardiff. (All the information can be inspected remotely or at either location.) However, that reciprocity is in some ways only superficial since the underlying law of property and rights of security is radically different in the two jurisdictions. However, if the recommendations were implemented there would be differences in the information publicly available to an inquirer:

- In England and Wales, the public record at Companies House would include financing statements that would disclose the possible existence of a charge or charges over a category of asset, or a particular asset but details would require to be sought from the company.
- In Scotland, the text of floating charges (and standard securities, which, with floating charges, constitute the vast bulk of registrable securities) would be publicly available at Registers of Scotland. And – if the option were taken up – brief details of all securities would be available in the annual return supplemented by updating information from the company; alternatively, the public record at Companies House would include brief particulars of floating charges and standard securities as provided by Registers of Scotland.

### **Option 3 Modify the existing scheme for England and Wales**

4.4.3.1 Under this option, many of the costs and problems of the existing scheme would be removed. Those that would continue would be those relating to:

- (a) the date of creation of the charge
- (b) the period of invisibility;
- (c) the complex position as regards priority of competing claims

- (d) the need for negative pledge and automatic crystallisation clauses
- (e) confusion about the position of those who buy unknowingly buy property that is the subject of security;
- (f) the quality of information on the record at Companies House ;
- (g) differences between the schemes for Scotland and for England and Wales
- (h) uncertainty relating to charges over financial collateral
- (i) Lack of information about receivables that have been sold; and
- (j) Barriers to receivables financing caused by prohibitions on assignment.

4.4.3.2 There might only be a partial reduction of the problems and costs associated with late registration.

4.4.3.3 In addition, there would be:

- transitional costs for lenders in adapting their systems and training their staff; and
- the costs of modifying the system at Companies House.

## **Other costs**

### **Costs for a typical business**

4.5 In practice, the direct affect on a typical company will be minimal. This is because the normal practice is for the secured party, ie the lender, to register a charge or security interest so as to ensure its validity against a creditor, administrator or liquidator. Companies will be directly affected by any change to the requirements for them:

- to maintain their own registers of charges;
- to allow inspection of their registers or copies of instruments creating charges;
- to include additional information in their Annual Returns.

See paragraphs 3.1.4, 3.3.A.2(x), 3.3.2.B.6, and 3.3.28.

4.6 Those who provide secured borrowing to companies will be directly affected by the proposals.

4.7 The proposals will also affect the costs of credit-reference agencies and others who use information about companies' financial strength will also be affected.

## **Consultation**

### **(i) within Government**

5.1 The DTI has consulted the Scottish Executive during the preparation of this partial RIA. The Insolvency Service, Companies House, the Land Registry, Registers of Scotland and the Patent Office were all involved in the consultation by the Law Commissions.

### **(ii) Public consultation**

5.2 Both Law Commissions consulted extensively during their reviews. Their consultation papers are available on their websites: [www.lawcom.gov.uk](http://www.lawcom.gov.uk) and [www.scotlawcom.gov.uk](http://www.scotlawcom.gov.uk). In addition, the English Commission held a series of seminars with stakeholders to consider specific issues.

## **Small Firms Impact Test**

6.3 The immediate impact is on lenders rather than borrowers. Therefore those who responded to Law Commissions' consultations were primarily lenders and their professional advisers. In October 2004, DTI sent a questionnaire to small 120 small companies that have volunteered to answer questions about financial services. Over half replied, of whom only 3 had an annual turnover exceeding £10million. The purpose of the questionnaire was to assess how small firms might be affected by the proposals. Key points arising from this limited consultation with these small companies were that:

- the vast majority factor their debts;
- nearly half have purchases subject to retention of title clauses and a similar proportion's sales are similarly subject.
- Of the companies based in England and Wales, few had assets in Scotland but nearly half had Scottish customers or suppliers;
- The number of Scottish companies in the group was too small for their answers about English assets, customers and suppliers to be useful;
- Over half had secured borrowing, with slightly more having a floating charge than a fixed charge;
- Most of those with secured borrowing considered that the terms of their loan had been influenced by their ability to offer security;

- About a third of those with secured borrowing said their lender had not taken responsibility for registering the charge;
- Most thought it would be helpful if the prepared version of the Annual Return sent to them by Companies House (the “shuttle”) were to include details of any secured lending to them that was registered;
- About half of those with secured borrowing kept a register of their charges;
- Only 11 companies answered the questions about the cost of updating information on the shuttle Annual Return or maintaining a register of charges. Several thought the amount negligible in both cases; 3 estimated costs of £100 and over for both, with the highest estimate being £200 for keeping the register of charges (from a company that does not currently maintain a register). A company that does maintain the register gave an estimate of £150 for both tasks.
- 2 companies had been the subject of request to inspect their registers of charges; a further 2 had had requests to inspect copies of the instruments creating the charges.

### **Competition assessment**

7.1 The Law Commission’s proposals affect the priority of competing charges, providing statutory rules that would remove uncertainty. The priority of preferential creditors and the unsecured creditors fund introduced by the Enterprise Act 2002 will not be affected.

7.2 The Scottish Law Commission’s proposals provide statutory rules for the priority of floating charges .

### **Enforcement, sanctions and monitoring**

8.1 The existing system , which would be retained under Option 1, is enforced primarily through the provision whereby a registrable charge is not valid against a creditor or an administrator or liquidator if not duly registered. This “sanction of invalidity” is extremely effective. In addition there are:

- a criminal sanction on the company and its officers if its charges are not duly registered; and
- a civil sanction on the company, whereby the secured amount is payable on demand if the charge is not duly registered;
- a criminal sanction on officers of the company if there are omissions from its own register of charges

- in the event of a company refusing to allow inspection of its charges register or copies of instruments creating a charge, a court may by order compel an immediate inspection.

8.2 Options 2 and 3 both retain:

- the sanction of invalidity for those charges registrable at Companies House, and
- the power for a court to compel an immediate inspection of copies of instruments.

The other sanctions would be abolished.

8.3 Under the recommendations of the Scottish Law Commission no sanction is necessary in relation to floating charges since only by registration in the register of floating charges could the inchoate security right be constituted. As respects the proposals for the annual return, the making of an accurate annual return is already a statutory responsibility of a company and the existing sanctions would continue to apply (but there are doubts as to effectiveness of this sanction). The obligation to provide updating information could be enforced, if necessary, by an order for specific performance in the civil courts.

## **ANNEX A Terms of Reference**

**The Law Commission** were asked:

- (1) to examine the law on the registration, perfection and priority of company charges;
- (2) to consider the case for a new scheme of registration and priority of company charges, including charges created by
  - a. companies having their registered office in England or Wales, wherever the assets charged are located; and
  - b. overseas companies and companies having their registered office in Scotland, where the charge is subject to English law;
- (3) to consider whether such a scheme should apply both to security in the strict sense and to "quasi-security" interests such as conditional sales, retention of title clauses, hire-purchase agreements and finance leases, including the extent to and means by which such interests should be made subject to the law governing securities;
- (4) to examine the law relating to the granting of security and "quasi-security" interests by unincorporated businesses and individuals over property other than land, including the feasibility of extending any new scheme for company charges to such interests, and the extent to and means by which such "quasi-security" interests should be made subject to the law governing securities; and
- (5) to make recommendations for reform.

**The Scottish Law Commission** were asked:

to examine the present scheme on the registration and priority of rights in security granted by companies and to make recommendations for its reform as it applies to

- (a) companies having their registered office in Scotland wherever the assets are located;
- (b) security granted under Scots law by overseas companies and companies having their registered office in England and Wales.

**ANNEX B.1 Draft Regulations to implement the recommendations of the  
Law Commission for England and Wales**

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**S T A T U T O R Y I N S T R U M E N T S**

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**2006 No. xxxx**

**COMPANIES**

**The Company Security Regulations 2006**

*Made* - - - -

*Laid before Parliament*

*Coming into force* - -

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The Secretary of State in exercise of the powers conferred on him by sections [x, y and z of the Companies Act 2006] hereby makes the following Regulations:

**PART 1**  
**INTRODUCTION**

*Citation and commencement*

**Citation and commencement**

- 1. These Regulations may be cited as the Company Security Regulations 2006.  
These Regulations come into force on [date].

## *Scope of the Regulations*

### **Companies registered in England and Wales**

—2. These Regulations apply to—

any charge or pledge created by a company registered in England and Wales over any of its property (wherever situated), and

any sale of receivables by a company registered in England and Wales.

If the property is situated in a jurisdiction outside England and Wales, these Regulations do not affect any right acquired in, or in relation to, the property in accordance with the law of that jurisdiction.

In these Regulations—

“charge” includes a mortgage,

“receivables” means monetary obligations, whether or not earned by performance, arising from—

- (a) the supply of goods or services (other than insurance services),
- (b) the supply of energy, or
- (c) brokerage fees, and

“sale”, in relation to receivables, includes an agreement to sell.

### **Other companies**

**3.**—(1) These Regulations also apply to any charge or pledge created by a company registered in Scotland, or by a company registered elsewhere than in Great Britain (a “foreign company”), over its property situated in England and Wales.

(2) For the purposes of paragraph (1)—

(a) an aircraft is treated as situated in England and Wales while it is registered in the UK Aircraft Register of Civil Aircraft maintained under the Air Navigation Order 2000<sup>(13)</sup>, even if it is not in England and Wales at the time in question, and

a ship is treated as situated in England and Wales while it is registered in Part 1, 2 or 3 of the register of British ships maintained under section 8(1) of the Merchant Shipping Act 1995<sup>(14)</sup>, even if it is not in England and Wales at the time in question;

but an aircraft or ship which is registered only under the law of any other jurisdiction does not fall within paragraph (1), even if it is in England and Wales at the time in question.

### **Exceptions**

—(b) These Regulations do not apply to—

a lien, charge or other interest arising under an enactment or rule of law,

the assignment of an unearned right to payment under a contract to a person who is to perform the transferor’s obligations,

the assignment of receivables solely to facilitate collection on behalf of the person making the assignment,

the assignment of a single receivable to an assignee in full or partial satisfaction of a pre-existing indebtedness,

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<sup>(13)</sup> S.I. 2000/1562.

<sup>(14)</sup> 1995 c. 21.

the sale of receivables as part of the sale of a business out of which the receivables arose,

a fixed charge which is registered, or the subject of a notice, under the Land Registration Act 2002<sup>(15)</sup>, or

a charge arising from the creation of a Lloyd's relevant trust fund, other than a Lloyd's deposit.

Paragraph (1) is subject to these Regulations and in particular to regulations 25 and 31 (which affect the priority of certain charges over land and liens).

## PART 2

### REGISTRATION OF CHARGES AND SALES OF RECEIVABLES

#### **The Register**

—(c) The Registrar of Companies (“the Registrar”) must establish and maintain a register of charges and of sales of receivables (“the register”).

An application for registration of a charge, or a sale of receivables, must be made by filing a financing statement that satisfies the requirements of these Regulations and the Rules.

The person filing a financial statement must confirm that the charge or sale to which it relates has been made or that the debtor consents to the filing.

A financing statement that does not meet the requirements of these Regulations or of the Rules may be rejected by the Registrar.

A financing statement may also be rejected by the Registrar if—

- (d) the prescribed filing fee is not paid, or
- (e) an arrangement for paying the filing fee is not in place.

In these Regulations—

“prescribed” means prescribed by the Rules,

“registered”, in relation to a charge or a sale of receivables, means (except in the context of registration in a specialist register in regulation 25) that a financing statement relating to it—

- (f) has been registered,
- (g) is not ineffective because of regulation 9 (errors), and
- (h) has not expired or been discharged,

and “unregistered” is to be read accordingly, and

“Rules” means rules made by the Registrar in accordance with section [x of the Companies Act 2006].

#### **Financing statement**

—(i) A financing statement—

may be filed before or after the charge or sale to which it relates is made,  
may relate to more than one charge or sale, and  
must include the required information.

The required information is—

the name of the debtor,  
the debtor's registered number (if any),

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<sup>(15)</sup> 2002 c. 9.

the name and address of the chargee or buyer, or its agent (if any),  
a description of the collateral,  
whether the filing is to continue indefinitely or until a specified date, and  
such other information as may be prescribed by the Rules.

(3) A financing statement may also disclose whether the chargee is a trustee.

(4) Paragraphs (2) and (3) are subject to regulation 9 (errors).

In these Regulations—

“chargee” means a person in whose favour a charge is created, including a trustee or any other party who holds a charge for the benefit of another person;

“collateral” means—

- (a) property subject to a charge or pledge, or
- (b) receivables that have been sold,

“debtor” means—

- (a) a company whose property is subject to a charge or pledge, whether to secure its own obligation or that of another,
- (b) a company which sells receivables, or
- (c) a transferee of, or successor to, a company falling within paragraph (a) or (b) of this definition, and

“registered number”, in relation to a company, has the same meaning as in the [Companies Act 2006].

### **When registration is effective**

—(5) A filed financing statement is registered when a date, time and number (“the financing statement number”) are assigned to it by the Registrar.

(6) The financing statement number determines the order of registration in the event of two or more financing statements being registered with the same date and time.

Registration continues to be effective—

until it is discharged, or

if the financing statement specifies a date on which registration is to end,  
and the registration has not by then been discharged, until that date.

(7) This is subject to regulation 9 (errors).

### **Verification statement**

—(8) As soon as is reasonably practicable after registration of a financing statement, the Registrar must send a statement (a “verification statement”) to—

the person (“P”) named in the financing statement as the chargee or buyer or  
its agent, and

the debtor.

But if the debtor is a foreign company which has not registered a place of business or branch in Great Britain under the [Companies Act 2006], the Registrar may instead require P to forward a copy of the verification statement to the debtor within 10 business days of receiving it.

Paragraph 1(a) does not apply if P has notified the Registrar in writing that he does not require copies of verification statements.

Paragraphs (1)(b) and (2) do not apply if the debtor has notified the Registrar in writing that he does not require copies of verification statements.

A verification statement must include—  
the information contained in the financing statement,  
the financing statement number, and  
the date and time of registration.

### **Errors in financing statement**

—(9) The registration of a financing statement is ineffective to register a charge or sale if it contains a defect such that its existence would not be discovered by a reasonable search under regulation 15.

But the registration is not otherwise affected by any defect in the financing statement.

If the debtor has changed its name, the fact that a person searching under its previous name might not discover the existence of the financing statement does not, of itself, make the registration ineffective.

Nothing in paragraph (1) requires a search to have been carried out.

Failure to provide a description in a financing statement in relation to any collateral does not make the registration ineffective with respect to other collateral described in the financing statement.

“Defect” includes an irregularity, omission or error.

### **Additional statements**

—(10) In these Regulations “additional statement” means a statement that satisfies the requirements of these Regulations and the Rules and is filed by the chargee or buyer or its agent under—

regulation 11 (extension or discharge of registration),  
regulation 12 (amendment of financing statement),  
regulation 13 (notice of transfer), or  
regulation 14 (notice of subordination),

or under regulation 16 (debtor etc may require additional statement).

An additional statement that does not meet the requirements of these Regulations or of the Rules may be rejected by the Registrar.

An additional statement may also be rejected by the Registrar if—

- (a) the prescribed filing fee is not paid, or
- (b) an arrangement for paying the filing fee is not in place.

### **Extension or discharge of registration**

—(c) The registration of a financing statement may, at any time before it expires, be extended or discharged by filing an additional statement.

A registration which is extended continues to have effect until—

the date specified in the additional statement, or  
if earlier, the date on which the registration is discharged.

### **Amendment of financing statement**

—(d) A registered financing statement may, at any time before it expires, be amended by filing an additional statement.

(11) The additional statement is registered when a date, time and number are assigned to it by the Registrar.

### **Notice of transfer**

—(12) If, in relation to a registered charge or registered sale, the chargee or buyer transfers an interest in collateral, an additional statement disclosing the transfer may be filed.

For the avoidance of doubt, the transferee of a registered charge, or of receivables which are the subject of a registered sale, is not required to file an additional statement in order to continue the effectiveness of the registration against an administrator or liquidator or a person mentioned in regulation 20(4) or 36(2) (execution creditors etc).

If an additional statement is filed under paragraph (1), and an interest in part of the collateral is transferred, the statement must include a description of the collateral in which the interest is transferred.

If, in relation to an unregistered charge or sale of receivables, the chargee or buyer transfers an interest in collateral, a financing statement may be filed in which the transferee is disclosed as the chargee or buyer.

An additional statement disclosing a transfer of a charge or of the sale of receivables may be filed before or after the transfer.

Once an additional statement is registered, the transferee is to be treated as the chargee or buyer for the purposes of these Regulations.

### **Notice of subordination**

—(13) If a charge or sale of receivables has been subordinated by the chargee or buyer to the interest of another person, an additional statement may be filed disclosing the subordination.

The additional statement may be filed at any time before the registration of the financing statement relating to the charge or sale expires.

### **Searches**

—(14) Any person may search the register, subject to any condition or exception imposed by the Rules, including in particular any requirement to pay a prescribed fee.

The register must be organised so as to permit searches using one or more of the following criteria—

the name of the debtor,

the registered number of the debtor (if any),

the financing statement number,

and any additional criteria permitted by the Rules.

A search result that purports to be authorised by the Registrar, whether printed by the Registrar or by any other person, may be received in evidence as prima facie proof of its contents.

### **Debtor etc may require additional statement**

—(15) If—

a financing statement is registered, and

one of the conditions set out in column 1 of the Table is satisfied,

the debtor, or any person with an interest in property which falls within the description of the collateral in the financing statement, may give a notice in writing (a “requirement notice”) to the person (“P”) named in the financing statement as chargee, buyer or its agent.

The requirement notice must—

- specify the condition which is satisfied,
- require P to file an additional statement with the effect indicated in column 2 of the Table relating to that condition, and
- inform P that failure to comply with the requirement notice may result in the person who gives the notice filing the appropriate additional statement.

**Table**

Additional statements

<i>1. Condition</i>	<i>2. Effect</i>
That the obligations under all of the charge agreements or sale agreements to which the financing statement relates have been performed.	To discharge the registration.
That the chargee or buyer has agreed to release part or all of the collateral described in the financing statement.	To amend or discharge the registration so as to reflect the terms of the agreement.
That the description of the collateral in the financing statement includes an item or kind of property that is not collateral under a charge agreement or sale agreement between the chargee or buyer and the debtor.	To amend the collateral description to exclude items or kinds of property that are not collateral under a charge agreement or sale agreement between the chargee or buyer and the debtor.
That no charge agreement or sale agreement exists between the persons named in the financing statement as the chargee or buyer and the debtor.	To discharge the registration or, where that debtor is not the sole debtor, to amend the registration.

If the person who gives a requirement notice is not the sole debtor, he must give a copy of the requirement notice to every other debtor to whom the financing statement relates within 5 business days of the requirement notice being given to P.

The person who gives a requirement notice may file an additional statement as requested in the requirement notice if P does not, within 15 business days after the notice is issued—

- comply with the requirement notice, or
- commence proceedings in the appropriate court for an order to maintain the registration to which the notice relates and notify the person who gave the requirement notice and the Registrar accordingly.

If the Registrar is notified under paragraph (4)(b) of the commencement of proceedings, he must, as soon as reasonably practicable, amend the register to show that the registration is the subject of a dispute.

On an application by P to the appropriate court, the court may order that the registration—

be maintained on any condition and for any period of time that the court considers appropriate, subject to regulations 7(3), 11(2) and 12 (duration, extension and amendment), or  
be discharged or amended.

If a court order is not obtained within 90 business days of the commencement of proceedings or such longer period as the court may direct, the person who gave the requirement notice may file an additional statement as requested in the requirement notice as if P had not complied with paragraph (4).

Paragraphs (4) to (7) do not apply to a trust case.

In a trust case, the appropriate court may, on an application by the person giving the requirement notice, make an order directing that the registration be amended or discharged if—

- (a) one or more of the conditions in paragraph (2) are satisfied, and
- (b) the chargee or its agent does not comply with the requirement notice within 25 business days after the notice is issued;

and the court may make such other orders as it thinks proper for the purpose of giving effect to the order.

In this regulation—

“the appropriate court” has such meaning as may be prescribed;

“trust case” means a case in which the financing statement discloses that the chargee is a trustee.

(16) Notices under this regulation must be given in the prescribed form and manner.

### **Entitlement to damages for incorrect filing etc**

—(17) If a person (without having a reasonable excuse)—

files a financing statement confirming the existence of a charge agreement or sale agreement which does not in fact exist, or

files a financing statement confirming that the debtor has consented to the filing when the debtor has not in fact consented,

the debtor has a right to recover damages from him for any loss or damage that was reasonably foreseeable as likely to result from the filing.

If a person (without having a reasonable excuse) fails to forward a copy of the verification statement to the debtor within 10 business days of receiving it as required under regulation 8(2) (verification statement), the debtor has a right to recover damages from him for any loss or damage that was reasonably foreseeable as likely to result from the filing.

### **Requirement to notify Registrar about appointment of receiver**

—(18) A person who—

obtains an order for the appointment of a receiver or manager of a company’s property, or

appoints a receiver or manager of a company’s property under powers contained in an instrument,

must notify the Registrar of that fact within 7 days of the order or appointment.

A receiver or manager of a company’s property appointed under powers contained in an instrument who ceases to act as such must, on so ceasing, notify the Registrar.

The Registrar must enter information notified under paragraph (1) and (2) in the register.

A notice under this section must be in the prescribed form and manner.

A person who fails to comply with this regulation is guilty of an offence and liable on summary conviction to a fine not exceeding level 3 and to a fine not exceeding one-tenth of that level for each day on which the failure continues.

### **Filing is not notice**

—(19) The filing of a financing statement or additional statement does not constitute notice or knowledge of its existence or contents to any person.

A purchaser of collateral is not required to enquire whether—

the collateral has been charged or pledged or, in the case of receivables, sold, or

whether the disposition constitutes a breach of the terms of the charge.

## **PART 3**

### **EFFECTIVENESS OF CHARGES ETC**

#### **Effectiveness of charge or sale of receivables in insolvency proceedings**

—(20) A charge or a sale of receivables is not effective against an administrator or liquidator unless, before the onset of insolvency,—

it is registered,

in the case of a supporting obligation, the charge over the obligation it supports is registered,

in the case of a right to the proceeds of collateral arising other than only as a result of the terms of a floating charge, if the charge over the original collateral is registered, or

in the case of a charge over sums due under a letter of credit, regulation 26(5) is satisfied.

Paragraph (1) does not apply in the case of a sale of receivables if the sale (by itself or in conjunction with other sales to the buyer) is of such a small proportion of the assignor's receivables that it would not influence a reasonable person deciding whether to make an advance to the company; and for the purposes of Part 4 (priority) such a sale of receivables is to be treated as having been registered at the date of the sale.

“Onset of insolvency” means—

if an administrator of a company is appointed by administration order, the date on which the administration application is made,

if an administrator of a company is appointed under paragraph 14 or 22 of Schedule B1 to the Insolvency Act 1986<sup>(16)</sup> (appointment of administrator by the holder of a qualifying floating charge, or by the company or its directors) following filing with the court of a copy of a notice of intention to appoint under that paragraph, the date on which the copy of the notice is filed,

if an administrator of a company is appointed otherwise than under sub-paragraph (a) or (b), the date on which the appointment takes effect,

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<sup>(16)</sup> 1986 c. 45.

if a company goes into liquidation, the date of the commencement of the winding-up.

A charge or interest arising under a sale of receivables is subordinate to the interest of a person—

who causes the collateral to be seized in accordance with due process to enforce a judgment, including execution, attachment or garnishment, or

who has obtained a charging order or equitable execution which affects or relates to the collateral,

unless the charge or sale falls within paragraph (1)(a) to (d) at the time that person's interest arises.

(21) This regulation does not apply to charges to which regulation 36 applies (effectiveness of charge over investment property or cash in insolvency proceedings).

### **Charges over imported goods**

—(22) Paragraph (2) applies to a charge over imported goods—

created by a company registered in Scotland or a foreign company, and

perfected under the law of any jurisdiction in which the goods were located (“the first jurisdiction”) before being imported.

For the purposes of these Regulations, a charge remains effective against an administrator or liquidator or a person mentioned in regulation 20(4) or 36(2) (execution creditors etc) if it is registered—

not later than 60 business days after the day on which the goods were imported, or

before perfection ceases under the law of the first jurisdiction,

whichever is the earlier.

For the purposes of Part 4 (priority), a charge which remains effective under paragraph (2) has priority from the date on which it was first perfected under the first jurisdiction.

But a charge which remains effective under paragraph (2) is subordinate to the interest of a transferee (other than a chargee or pledgee) who takes possession or delivery of the goods—

after the goods have been imported,

without knowledge of the charge, and

before the charge is registered.

“Imported” means brought into England and Wales.

“Perfected”, in relation to a charge, means that all necessary steps have been taken to render it effective against third parties and in insolvency proceedings under the law of the jurisdiction in question; and “perfection” has a corresponding meaning.

### **Pledge treated as charge if collateral made available to debtor**

—(23) This regulation applies to a pledge of a negotiable instrument (including a certificated financial instrument in bearer form) which the pledgee delivers to the debtor for the purpose of –

sale or exchange,

presentation, collection, enforcement, renewal, or registration of a transfer.

This regulation also applies to a pledge of—

a negotiable document of title to goods, or  
goods held by a bailee which are not covered by a negotiable document of  
title,

if the pledgee makes the document of title or goods available to the debtor for any of the purposes  
mentioned in paragraph (3).

The purposes are—

sale or exchange,  
loading, unloading, storing, shipping, transshipping, manufacturing,  
processing, packaging or otherwise dealing with goods in a manner  
preliminary to their sale or exchange.

For the period during which the collateral is made available to the debtor, a pledge to  
which this regulation applies and any right of the pledgee to the proceeds of  
disposition of the collateral is treated as a charge over the collateral and its  
proceeds which, for the first 15 business days of that period, need not be  
registered to be effective against an administrator or liquidator or a person  
mentioned in regulation 20(4) or 36(2) (execution creditors etc).

For the purposes of Part 4 (priority) and without prejudice to regulation 39 (special  
priority rules for investment property and cash), a pledge to which this  
regulation applies has priority from the date it was created if—

the collateral is returned or the proceeds transferred to the pledgee within  
the 15 day period mentioned in paragraph (4), or  
it is registered as a charge within that 15 day period and remains registered  
until the collateral is returned or the proceeds transferred to the pledgee.

#### **Attornment by debtor**

**4.** These Regulations apply to a pledge under which the debtor has possession of collateral and  
attorns to the pledgee as if the pledge were a charge.

## **PART 4**

### **PRIORITY**

#### *Priority rules*

#### **Residual rules**

—5. The following provisions apply if these Regulations do not otherwise determine priority  
between conflicting charges, sales of receivables and pledges.

A registered charge or sale of receivables has priority over an unregistered charge or  
sale of receivables.

Priority between registered charges and registered sales of receivables is determined  
by the order of registration of the relevant financing statements.

Priority between unregistered charges and unregistered sales of receivables is  
determined by the order of creation or sale.

Priority between a charge and a pledge is determined by whether the financing  
statement relating to the charge is registered before the pledge is created.

A transferee of a charge or pledge acquires the same priority with respect to the  
charge or pledge as the transferor had at the time of transfer.

A charge over, or sale of, a supporting obligation has the same priority as the charge  
over, or sale of, the principal obligation which it supports.

Any right to the proceeds of collateral arising other than only as a result of the terms of a floating charge has the same priority as the charge over the original collateral.

(1) A registered charge over crops growing on land has priority over a conflicting interest in the land if the debtor has an interest in or is in occupation of the land.

The priority that a charge, pledge or sale of receivables has under this regulation applies to all advances, including future advances, whether or not made under an obligation.

Paragraph (10) applies to give a registered charge or a pledge priority over the interests of persons mentioned in regulation 20(4) (execution creditors etc) only to the extent of—

advances made before—

the interests of those persons arise, or

those persons seize the collateral or obtain a right to it,

advances made before the chargee or pledgee acquires knowledge of the interests of those persons,

advances made under—

a statutory requirement, or

a legally binding obligation which was entered into by the chargee or pledgee before acquiring the knowledge mentioned in subparagraph (b), and

(a) such costs and expenses as were provided for in the charge or pledge agreement or, in the absence of such agreement, reasonable costs and expenses incurred by the chargee or pledgee for the protection, preservation, maintenance or repair of the collateral.

For the purposes of this regulation, the priority of a contractual lien dates from—

the agreement for the lien, or

the date on which the goods come into possession of the lienee,

whichever is later.

“Advance” means the payment of money, the provision of credit or other giving of value, and includes any entitlement to interest, credit costs and other charges or costs payable in connection with an advance or the enforcement of a charge or pledge securing the advance.

### **Conflict with transactions registered in specialist registers**

—(b) Any conflict between—

a registered or unregistered charge, and

a transaction which is registered in a specialist register,

is to be determined in accordance with the priority rules in the enactments governing the specialist register, subject to paragraphs (2) to (4).

If the conflict is between—

(c) a floating charge created by a company over unregistered land and any other charge over the same land, or

(d) a floating charge created by a company over registered land and any other transaction over the same land except a legal purchase,

the floating charge has priority if the financing statement relating to it was registered under these Regulations before the competing transaction was registered in the specialist register or the financing statement relating to it was registered under these Regulations.

(2) If the conflict is between a fixed equitable charge created by a company over registered land and any other transaction over the same land other than a legal mortgage or other legal purchase, the fixed equitable charge has priority if it was registered in the specialist register or the financing statement relating to it was registered under these Regulations before the competing transaction was registered in the specialist register or the financing statement relating to it was registered under these Regulations.

(3) Paragraphs (2) and (3) are without prejudice to sections 28 to 30 of the Land Registration Act 2002<sup>(17)</sup> (effect of dispositions on priority) and rules 147 to 154 of the Land Registration Rules 2003<sup>(18)</sup> (official searches with priority).

“Specialist register” means a register established under any of the following enactments—

- the Land Charges Act 1972<sup>(19)</sup>,
- the Land Registration Act 2002,
- the Merchant Shipping Act 1995<sup>(20)</sup>,
- the Mortgaging of Aircraft Order 1972<sup>(21)</sup>,
- the Patents Act 1977<sup>(22)</sup>,
- the Registered Designs Act 1949<sup>(23)</sup>, and
- the Trade Marks Act 1994<sup>(24)</sup>.

### **Sums due under letters of credit**

—(4) The following provisions govern priority between conflicting charges over the same sums due under a letter of credit.

A charge held by a chargee who has command of the sums due under the letter of credit has priority over a conflicting charge held by a chargee who does not have command.

Conflicting charges under which each chargee has command rank according to priority in time of obtaining command.

In all other cases, priority among conflicting charges in the same sums due under a letter of credit is governed by regulation 24 (residual priority rules).

A chargee has command of the sums due under a letter of credit to the extent of any right to payment or performance by the issuer or any nominated person—

where the issuer or nominated person is bound or compelled under any enactment, instrument or rule of law to receive notice of an assignment or charge, if the chargee has notified the issuer or nominated person of its assignment of, or fixed charge over, the sums due under the letter of credit, or

if the issuer or nominated person is not so bound or compelled, the chargee has obtained the agreement of the issuer or nominated person that the debtor will no longer be able to deal with the sums due under the letter of credit without the agreement of the chargee.

“Nominated person” means a person whom the issuer—

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<sup>(17)</sup> 2002 c.9.  
<sup>(18)</sup> S.I. 2003/1417.  
<sup>(19)</sup> 1972 c. 61.  
<sup>(20)</sup> 1995 c. 21.  
<sup>(21)</sup> S.I. 1972/1268.  
<sup>(22)</sup> 1977 c. 37.  
<sup>(23)</sup> 1949 c. 88.  
<sup>(24)</sup> 1994 c. 26.

designates or authorises to pay, accept, negotiate or otherwise give value under a letter of credit, and undertakes by agreement or custom and practice to reimburse.

#### *Transfers*

#### **Priority of charges in transferred collateral**

—(5) If the debtor acquires property subject to a charge (“charge A”) created by a company other than the debtor, charge A has priority over any charge over the same property created by the debtor if—

charge A was registered when the debtor acquired the collateral, and there is no period after the debtor acquired the collateral when charge A was not registered.

If the debtor acquires property subject to a charge created by a person who is not a company, that charge has priority over any charge over the same property created by the debtor.

Paragraphs (1) and (2) are subject to regulations 30 (protection of transferees of money, negotiable instruments etc), 38 (purchaser takes free: investment property) and 39 (special priority rules for investment property and cash).

#### **Transfer of collateral free of unregistered charge**

—(6) A transferee of collateral subject to an unregistered fixed charge who—

- (a) gives value, and
- (b) if the collateral is tangible, takes possession or delivery of it,

takes free of the charge unless he has knowledge of its existence.

For the purposes of paragraph (1), a transferee of a negotiable instrument or the holder of a negotiable document of title, who acquired the negotiable instrument or negotiable document of title in a transaction which was in the ordinary course of the transferor's business, has knowledge of the charge only if the transferee or holder acquired the interest with knowledge—

of the existence of the charge, and that the transaction is in breach of the terms of the charge.

A transferee of collateral subject to a unregistered floating charge, who acquired the collateral in a transaction which was in the ordinary course of the transferor's business, takes free of the charge unless the transferee knew that the transfer was in breach of the terms of the floating charge.

Paragraph (3) applies regardless of whether the charge was, as created, a floating charge or a fixed charge.

For the purposes of this regulation—

a charge falling within regulation 20(1)(b) or (c) or regulation 36(1)(e) or (f) (supporting obligation and proceeds) is to be treated as registered;

“transferee” does not include chargee, pledgee or buyer of receivables.

This regulation does not apply to a transfer which is in total or partial satisfaction of a money debt or antecedent liability.

#### **Circumstances in which transferee takes collateral free of registered charge**

—(c) A transferee of collateral subject to a registered charge which is a fixed charge takes subject to the charge unless the chargee has authorised the transfer.

A transferee of collateral subject to a registered charge which—

as created was a floating charge, or  
as created was a fixed charge but has become a floating charge,  
and who acquired the collateral in a transaction which was in the ordinary course of the transferor's business, takes free of the charge unless the transferee knew that the transfer was in breach of the terms of the floating charge.

For the purposes of this regulation—

a charge falling within regulation 20(1)(b) or (c) or regulation 36(1)(e) or (f)  
(supporting obligation and proceeds) is to be treated as registered;

“transferee” does not include chargee, pledgee or buyer of receivables.

This regulation does not apply to a transfer which is in total or partial satisfaction of a money debt or antecedent liability.

### **Protection of transferees of money, negotiable instruments etc**

Nothing in these Regulations affects the rights of a transferee of—

(d) money or other form of payment, or  
a negotiable instrument or negotiable document of title.

*Miscellaneous*

### **Priority: liens**

Any lien which arises by operation of law takes priority over a charge, whether or not registered.

### **Distress for rent or rates**

—(e) A landlord's right to distrain on goods for unpaid rent takes priority over any charge, whether or not registered.

A registered charge has priority over a local authority's right to distrain on goods for unpaid rates under Part 3 of the Non-Domestic Rating (Collection and Enforcement) (Local Lists) Regulations 1989<sup>(25)</sup> (or any equivalent regulations replacing Part 3).

### **Effect on priority of mistaken discharge of filing**

—(f) This regulation applies if registration of a charge or a sale of receivables is discharged by mistake or without authorisation.

If the chargee or buyer renews the registration in accordance with the Rules within 30 business days after the discharge, the discharge does not affect the priority ranking of the charge or sale to which the discharged registration relates as against a competing registered charge or sale which, immediately before the discharge, had a subordinate priority ranking.

But paragraph (2) does not apply to the extent that the competing registered charge or sale secures advances made or contracted for after the discharge and before renewal of the registration.

### **Voluntary subordination**

—(g) These Regulations do not preclude subordination by a person entitled to priority.

But subordination does not, of itself, create a charge.

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<sup>(25)</sup> SI 1989/1058; Part III was amended by the Non-Domestic Rating (Collection and Enforcement) (Local Lists) (Amendment) (England) Regulations 2003 (SI 2003/2210).

## **Rights of assignees**

—(h) In this regulation, “assignee” includes a chargee, buyer of receivables and a receiver.

Unless an account debtor has made an enforceable agreement not to assert defences to claims arising out of a contract, the rights of an assignee of the receivables are subject to—

the terms of the contract between the account debtor and the assignor and any defence or claim arising from the contract or a closely connected contract, and

any other defence or claim of the account debtor against the assignor which accrues before the account debtor acquires knowledge of the assignment.

(7) Any payment made by the account debtor to the assignor before receiving notice of the assignment of receivables discharges his obligation to the extent of the payment.

Payment by an account debtor to an assignee in accordance with a notice mentioned in paragraph (3) discharges the obligation of the account debtor to the extent of the payment.

A term in a contract between an account debtor and an assignor which prohibits or restricts assignment of the whole of the receivables for money due or to become due—

is binding on the assignor, but only to the extent of making the assignor liable in damages for breach of contract, but

is ineffective against assignees.

## **PART 5**

### **FINANCIAL COLLATERAL**

#### **Effectiveness of charge over investment property or cash in insolvency proceedings**

—(8) A charge over investment property or cash is not effective against an administrator or liquidator unless, before the commencement of winding-up proceedings—

it is registered,

(a) the charge is a security financial collateral arrangement,

(b) the chargee has control of the collateral,

the charge is in favour of an intermediary under regulation 37,

in the case of a supporting obligation, the charge over the obligation it supports is registered or is under the control of the chargee, or

in the case of any right to the proceeds of collateral arising other than only as a result of the terms of a floating charge, if the charge over the original collateral is registered or under the control of the chargee.

A charge over investment property or cash is subordinate to the interest of a person—

who causes the collateral to be seized in accordance with due process to enforce a judgment, including execution, attachment or garnishment, or

who has obtained a charging order or equitable execution which affects or relates to the collateral,

unless the charge falls within paragraph (1)(a) to (f) at the time that person’s interest arises.

- (9) “Security financial collateral arrangement” and “winding-up proceedings” have the meanings given in the Financial Collateral Arrangements (No. 2) Regulations 2003<sup>(26)</sup>.

### **Automatic charge in favour of intermediary etc**

—(10) A fixed charge in favour of an intermediary arises over a person’s financial assets held with the intermediary if—

the person buys the financial assets through the intermediary in a transaction in which the person is obliged to pay the purchase price to the intermediary at the time of the purchase, and

the intermediary credits the financial assets to the buyer’s securities account before the buyer pays the intermediary.

The charge described in paragraph (1) secures the person’s obligation to pay for the financial assets.

A floating charge in favour of a person who delivers a certificated financial instrument or other financial asset represented by a document arises over those financial assets if—

the financial assets are—

in the ordinary course of business transferred by delivery with any necessary endorsement or assignment, and

delivered under an agreement between persons in the business of dealing with such financial assets, and

the agreement calls for delivery against payment.

The charge described in paragraph (3) secures the obligation to make payment for the financial assets.

### **Purchaser takes free: investment property**

—(11) A purchaser of a certificated financial instrument in bearer form who—

gives value, and

obtains possession of the instrument,

without knowing that the purchase constitutes a breach of the terms of a charge which was created or provided for over the instrument, acquires the instrument free of the charge.

A purchaser of a certificated financial instrument in registered form or of an uncertificated financial instrument who—

gives value, and

is registered as the holder of the instrument,

without knowing that the purchase constitutes a breach of the terms of a charge which was created or provided for over the instrument, acquires the instrument free of the charge.

If a person who acquires a financial asset held with an intermediary which is transferred to an account held in that person’s name—

gives value, and

at the time of the transfer does not know that the acquisition constitutes a breach of the terms of the charge,

that person acquires the asset free of the charge.

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<sup>(26)</sup> S.I. 2003/3226.

## **Special priority rules for investment property and cash**

—(12) Subject to regulation 38 (purchaser takes free: investment property), the following provisions govern priority between conflicting charges or pledges over the same investment property or cash.

A charge or pledge under which the chargee or pledgee has control of the investment property or cash has priority over a charge or pledge under which the chargee or pledgee does not have control.

Conflicting charges under which each chargee has control of the investment property or cash rank according to the order in which control was acquired.

Conflicting charges granted by an intermediary under which the chargee does not have control rank equally.

In all other cases, priority among conflicting charges over investment property or cash is governed by regulation 24 (residual priority rules).

Regulation 24(10) and (11) apply to charges and pledges over investment property and cash with the following modifications—

- (a) the reference to a registered charge or pledge includes one under the control of the chargee or pledgee, and
- (b) the reference to persons mentioned in regulation 20(4) includes persons mentioned in regulation 36(2) (judgment creditors etc).

## **Meaning of “control”**

**6.**—(1) A chargee or pledgee has control of collateral in the cases set out in paragraphs (2) to (9), but only if—

the charge or pledge, and

the arrangement under which the chargee or pledgee has control of the collateral,

are evidenced in writing or by the recording (by electronic means) of a conversation.

(2) A chargee or pledgee has control of a certificated financial instrument in bearer form if he obtains possession of the certificate and the debtor has not regained possession.

A chargee has control of a certificated financial instrument in registered form if he—

has possession of the certificate, or

is registered with the issuer as the holder.

A chargee has control of an uncertificated financial instrument held in a settlement system if—

the operator of the system, on the instructions of the registered holder, has credited the financial instrument to a sub-account in the holder’s own name but the holder has given the chargee a power of attorney over the financial instrument,

the operator of the system is only permitted to effect a transfer of title to the financial instrument on the instructions of the chargee or a person acting on the chargee’s behalf and attributable to the debtor,

entry in the register maintained by or on behalf of the operator of the system determines legal title and the chargee is entered in that register as the holder, or

entry in the register maintained by or on behalf of the issuer determines legal title and the chargee is entered in that register as the holder.

A chargee has control of financial assets held with an intermediary—

if the assets are transferred to an account held by the chargee,  
where the intermediary is bound or compelled under any enactment,  
instrument or rule of law to receive notice of an interest in financial  
assets held with it, if the intermediary has been given notice of the  
assignment by way of mortgage or of a fixed charge, or

where the intermediary is not so bound or compelled, if the chargee has  
obtained the intermediary's agreement that the debtor will no longer be  
able to deal with the collateral without the agreement of the chargee.

If an interest in financial assets held with an intermediary is granted by an account  
holder to the account holder's own intermediary, the intermediary has control.

If a cash debtor is the chargee of cash it has control of the cash.

Any other chargee with a fixed charge over cash has control of the cash—

where the cash debtor is bound or compelled under any enactment,  
instrument or rule of law to receive notice of an interest in cash held  
with it, if the chargee notifies the cash debtor of the fixed charge,

(a) where the cash debtor is not so bound or compelled, if the  
chargee has obtained the cash debtor's agreement that the debtor will no  
longer deal with the collateral, or

if, with the agreement of the cash debtor and the debtor, the cash is  
transferred into the chargee's name.

In a case not falling within any of paragraphs (2) to (8), a chargee or pledgee has  
control of collateral consisting of investment property or cash if the debtor is no  
longer able to deal with the collateral.

If a charge extends to after-acquired investment property held in a securities account  
or cash, control over the after-acquired investment property or cash runs from  
the time control was first obtained over investment property held in that account  
or the cash subject to the charge.

Any right of the debtor to substitute equivalent collateral or withdraw excess  
collateral does not, of itself, prevent investment property or cash being held  
under the control of the chargee or pledgee.

A chargee who appoints a receiver under a power granted by the charge agreement  
does not thereby have control.

## **Meaning of other expressions used in Part 5**

—(b) In these Regulations—

“account holder” means a person in whose name an intermediary maintains a securities  
account;

“cash” means money (in any currency) credited to an account, or a similar claim for  
repayment of money and includes money market deposits and sums due or payable to, or  
received between, the parties in connection with the operation of a financial collateral  
arrangement or close-out netting provision (as defined in regulation 3 of the Financial  
Collateral Arrangements (No. 2) Regulations 2003<sup>(27)</sup>);

“cash debtor”, in relation to a debtor, means a person who owes cash to the debtor.

“certificated financial instrument” means a financial instrument represented by a certificate;

“deal with”, in relation to collateral, means that the debtor is no longer able to dispose of the  
collateral free of the chargee's or pledgee's interest or so as to give a purchaser an interest  
ranking in priority to that of the chargee or pledgee;

“financial asset” means—

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<sup>(27)</sup> S.I. 2003/3226.

- (a) a financial instrument,
- (b) an obligation of a person or a share, participation or other interest in a person or in property or an enterprise of a person—
  - (i) which is, or is of a type, dealt in or traded on financial markets, or
  - (ii) which is recognised in any area in which it is issued or dealt in as a medium for investment,
- (c) any property which is held by an intermediary for another person in a securities account if the intermediary has expressly agreed with the other person that the property is to be treated as a financial asset under these Regulations, or
- (d) a commodity futures contract, a commodity futures option or other similar contract;

“financial instrument” means—

- (a) a share in a company or any other financial instrument equivalent to a share in a company,
- (b) a bond or other form of financial instrument giving rise to or acknowledging indebtedness which is, or is of a type, dealt in or traded on financial markets, and
- (c) any other financial instrument which is normally dealt in and which gives the right to acquire any such share, bond, instrument or other security by subscription, purchase or exchange or which gives rise to a cash settlement (excluding an instrument of payment),

and includes a unit of a collective investment scheme within the meaning of the Financial Services and Markets Act 2000<sup>(28)</sup>, an eligible debt security within the meaning of the Uncertificated Securities Regulations 2001<sup>(29)</sup>, a money market instrument, an uncertificated unit of an interest in a security as defined in the Uncertificated Securities Regulations 2001, and any rights, privileges or benefits attached to or arising from any of the financial instruments included in this definition;

“intermediary” means a person who maintains registers or accounts to which financial assets may be credited or debited for others, or both for others and for his own account, but does not include—

- (a) a person who acts as a registrar or transfer agent for the issuer of financial instruments, or
- (b) a person who maintains registers or accounts in the capacity of operator of a system for the holding and transfer of financial instruments on records of the issuer or other records which constitute the primary record of entitlement to financial instruments as against the issuer;

“investment property” means a financial instrument, whether certificated or uncertificated and a financial asset held with an intermediary;

“securities account” means an account maintained by an intermediary to which financial assets may be credited or debited;

“settlement system” means a system for the holding and transfer of financial instruments on records of the issuer or other records which constitute the primary record of entitlement to financial instruments as against the issuer;

“uncertificated financial instrument” means a financial instrument not represented by a certificate.

A reference in these Regulations to a financial asset held with an intermediary means the rights of an account holder resulting from a credit of the financial asset to a securities account.

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<sup>(28)</sup> 2000 c. 8.  
<sup>(29)</sup> S.I. 2001/3755.

PART 6  
MISCELLANEOUS AND SUPPLEMENTARY

**Interpretation: general**

**7. In these Regulations—**

“business day” means any day which is not—

- (a) a Saturday or Sunday,
- (b) a bank holiday, or
- (c) Christmas Day or Good Friday;

“company” has the meaning given in [the Companies Act 2006];

“crops” means crops, whether matured or otherwise, and whether naturally grown or planted, attached to land by roots or forming part of trees or plants attached to land, but does not include trees;

“document of title” means a document written on paper issued by or addressed to a bailee—

- (a) which covers goods in the bailee's possession that are identified or are unascertained portions of an identified mass, and
- (b) in which it is stated that the goods identified in it will be delivered to a named person, or to the transferee of that person, or to bearer or to the order of a named person;

“goods” means tangible property including fixtures, crops, trees which have been severed and the unborn offspring of animals, but does not include a document of title, a negotiable instrument, investment property which is represented by a certificate, money or minerals falling within the definition of land under the Land Registration Act 2002<sup>(30)</sup> or the Land Charges Act 1972<sup>(31)</sup>;

“Lloyd’s deposit” means any funds held on trust pursuant to a Lloyd’s deposit trust deed or a Lloyd’s security and trust deed;

“Lloyd’s relevant trust fund” means any funds held on trust under a trust deed entered into by the member in accordance with the requirements of the Authority and Byelaws of the Society for the payment of an obligation arising in connection with insurance market activity carried on by a member, or for the establishment of a Lloyd’s deposit, and includes funds held on further trusts declared by the Society or the trustee of such a trust deed in respect of any class of insurance market activity;

“money” means notes and coins which are legal tender in any currency;

“negotiable instrument” means—

- (a) a cheque, bill of exchange or promissory note within the meaning of the Bills of Exchange Act 1882<sup>(32)</sup>, or
- (b) any other document written on paper which evidences a right to payment of money and is of a type which, in the ordinary course of business, is transferred by delivery with any necessary endorsement or assignment,

but does not include a document of title or investment property;

“pledge” includes a contractual lien;

“purchase” means take by sale, lease, discount, assignment, negotiation, charge, pledge, issue, reissue, gift or any other consensual transaction that creates an interest in property; and

“purchaser” has a corresponding meaning;

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<sup>(30)</sup> 2002 c. 9.  
<sup>(31)</sup> 1972 c. 61.  
<sup>(32)</sup> 1882 c. 61.

“supporting obligation” means a right to the sums due under of a letter of credit or a guarantee or indemnity which supports the payment or performance of the principal obligation under receivables, a document of title, a negotiable instrument or investment property;

“value” means any consideration which is sufficient to support a simple contract, and includes an antecedent debt or other obligation.

### **Index of defined terms**

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value	42
verification statement	8(1)

### **Account debtors and cash debtors**

—8. A person who owes receivables (an “account debtor”) may take a charge over the receivables.

A cash debtor may take a charge over the cash it owes.

### **Consequential amendments**

—9. [*Apply these Regulations to LLPs as they apply to companies by adding a reference to them in the Limited Liability Partnerships Regulations 2001 (S.I. 2001/1090) [and the Limited Liability Partnerships (Scotland) Regulations 2001 (S.I. 2001/128.)]*

Section 245 of the Insolvency Act 1986<sup>(33)</sup> (avoidance of certain floating charges created before onset of insolvency) shall be amended as follows.

In subsection (2), for the word “created” substitute “created or registered”.

In the opening words of subsection (3), for the word “created” substitute (in both places) “created or registered”.

In the opening words of subsection (4), for the word “creates” substitute “creates or registers”.

At the end of that section add—

“(7) In this section, “registered” means registered under the Company Security Regulations 2006”; and “registers” shall be construed accordingly.”

*[A number of other consequential amendments (other than cross-references and minor amendments) are identified in the Explanatory Note.]*

### **Transitional provisions and savings**

—10. In this regulation—

“commencement” means the date when these Regulations come into force,

“pre-commencement registered charge” means a charge which was registered under Part 12 of the Companies Act 1985<sup>(34)</sup> (certain charges void if not registered);

“pre-commencement sale of receivables” means a sale of receivables made before commencement which, had it been made after commencement, could have been registered under these Regulations;

“pre-commencement unregistrable charge” means a charge created before commencement which was not registrable under Part 12 of the Companies Act 1985 but which, had it been created after commencement, could have been registered under these Regulations;

“transitional period” means the period beginning with the date of commencement and ending two years later.

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<sup>(33)</sup> 1986 c. 45.

<sup>(34)</sup> 1985 c. 6.

(1) Rules may make special transitional provision for cases where the process of registration under Part 12 of the Companies Act 1985 was begun but not completed before commencement.

On commencement, a pre-commencement registered charge—

is to be treated as a registered charge,

retains its priority as against other pre-commencement registered charges, pre-commencement unregistrable charges, pledges and interests arising under pre-commencement sales of receivables, and

is subject to the priority rules in these Regulations as against other charges, pledges and interests arising under sales of receivables.

On commencement, a pre-commencement unregistrable charge—

retains its priority as against other pre-commencement registered charges, pre-commencement unregistrable charges, pledges and interests arising under pre-commencement sales of receivables,

has priority as if it had been registered at commencement, and

is subject to the priority rules in these Regulations as against other charges, pledges and interests arising under sales of receivables.

Except for paragraphs (2) to (7), these Regulations do not apply to a pre-commencement sale of receivables until after the end of the transitional period.

During the transitional period, the interest arising under a pre-commencement sale of receivables has priority over any conflicting charge created, or interest arising under a sale of receivables made, after commencement, whether or not registered.

If a pre-commencement sale of receivables is registered before the end of the transitional period, the commencement date is treated as the date of registration.

Date

Secretary of State

#### **EXPLANATORY NOTE**

*(This note is not part of the Regulations)*

*[to be inserted]*

**INTRODUCTION**

The draft Company Security Regulations 2006, which would be made under powers to be taken in the Companies Bill, provide a scheme for electronic registration of company charges and associated rules of priority. The Regulations would replace Part XII of the Companies Act 1985.

There is wide agreement that the current system for registration is out of date and needlessly expensive to operate. For example, documentation must be submitted to the Registrar of Companies in paper form. It must be checked by Registry staff before a Certificate of Registration is issued. A certificate must be obtained before a mortgage over land can be registered, which is hindering the development of electronic conveyancing. Charges must be registered within a 21-day period, which results in substantial costs when, as regularly happens, charges are not registered on time. The list of registrable charges is out of date and the requirements for charges created by overseas companies over their assets in England and Wales are defective.

The registration scheme was not designed to solve issues of priority between creditors and buyers or between different creditors with an interest in the same security. However, the current system has a major impact on priority rules. This is because a charge that is not registered within 21 days is void against other creditors and because registration of a charge has been held to give constructive notice to others. The rules on priority are both unclear in their operation and unsuited to the needs of modern company finance.

The Regulations permit the introduction of a wholly electronic system under which a lender taking a charge over a company's property will 'file' brief particulars of the charge on-line to the registry. Parties will no longer submit charge documents and the Registrar will no longer have to employ staff to check the particulars. The party filing will be responsible for ensuring that the information about the charge is accurate. The on-line system will be designed to minimise the chances of error and, if property is accidentally omitted, the charge will still be effective in respect of the property that was included in the particulars.

Registration will take place, and information will be available for on-line searching, almost instantaneously. The system will provide fuller information than the current register, as any charge will be registrable unless specifically exempted. This will include all non-exempt charges created by overseas companies over their assets in England and Wales. Charges over registered land that are registered at the Land Registry will no longer have to be registered at Companies House as well; the

relevant information will be sent automatically to the Company Security Register so that it is available to searchers.

Registration will no longer be compulsory and there will be no time limit. But if the company becomes insolvent before a charge has been registered, the charge will be ineffective as against the administrator or liquidator. It may also be invalidated if the filing was made shortly before the insolvency. Until it has been registered, a charge may lose its priority to a subsequent charge, as priority will depend primarily on the date of filing. An unregistered charge will not be effective against a person who buys the property unless they know of the charge.

The effectiveness of floating charges will be enhanced. Their essential characteristic, that the company remains free to dispose of its assets in the ordinary course of business, is preserved. However it will no longer be necessary to employ negative pledge clauses to preserve the priority of a floating charge against subsequent charges. Nor will it be necessary to use automatic crystallisation clauses to prevent seizure of the property by other creditors. Both types of clause are unreliable in their operation and add significantly to the complexity of the current law.

There are special provisions for charges over 'financial collateral' such as investment property and funds in bank accounts. The provisions complement the Financial Collateral Arrangements (No 2) Regulations 2003 and other legislation affecting financial collateral. They set out clear rules as to the priority of charges where the chargee takes 'possession or control' of the financial collateral instead of registering, and on when a person who purchases financial collateral without knowing of the charge will be affected by it. These provisions are essential to maintain the ready transferability of financial collateral.

For many companies, receivables are a major asset and sales of their receivables, for example to a factor or discounter, are a more important way of raising finance than creating charges. It is difficult for financiers and others to discover whether companies have sold their receivables. The rules of priority, which depend on the order in which notice is given to the debtor from whom the receivable is due, are unsuited to modern receivables financing. The Regulations provide for registration of sales of receivables. Their priority will depend on the order in which they are registered. The Regulations also provide that a term in the contract that gives rise to the receivable purporting to prohibit its assignment will be of no effect against the assignee. This removes a serious but often unintended obstacle to many small companies obtaining receivables financing.

The Regulations have been drafted on the assumption that the recommendations of the Scottish Law Commission in its Report on Registration of Rights in Security by Companies (Scot Law Com No 197, 2004) will be implemented.

The Regulations normally define a term on the first occasion on which it is used. Regulation 43 provides an index showing where the definitions of any defined term will be found.

## **PART 1                      INTRODUCTION**

### **Citation and Commencement**

#### **Regulation 1                      Citation and Commencement**

The title ‘Company Security Regulations’ reflects the fact that the Regulations apply not only to charges but also to pledges (dealing with their priority as against charges) and to sales of receivables.

### **Scope of the Regulations**

Regulations 2-4 deal with the scope of the Regulations.

#### **Regulation 2                      Companies registered in England and Wales**

The scheme applies to charges over the assets of a company registered in England and Wales, and to sales of its receivables.

It is immaterial whether a charge that is created by a company secures its own obligation or those of a third person (regulation 6(5) ‘debtor’). It is equally immaterial whether or not the chargee is a company. For the purposes of the Regulations, a person who holds security as trustee for a number of others is treated as the chargee (regulation 6(5) ‘chargee’).

The Regulations apply wherever the asset is situated (whether physically or, with intangible assets, according to the rules of private international law). In this the Regulations follow the Companies Act 1985, section 395. However regulation 2(2) reflects the position in practice that interests recognised by the law of the place where the asset is ‘situated’ will be frequently be given effect by that law regardless of whether the charge should have been registered in England and Wales. (Under current law this is required when article 5 of the Insolvency Regulation<sup>35</sup> applies.) Note that the Regulations are subject to various exceptions set out in regulation 4.

This regulation includes the definition of ‘receivables’, since the sales of receivables by companies registered in England and Wales will need to be registered to be effective (regulation 20). Priority will depend on date of registration (regulation 24.) The definition is a deliberately narrow one. The requirement to register sales of receivables applies only to the kinds of monetary obligation that are commonly sold by companies to factors or discounters. It does not apply, for example, to

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<sup>35</sup> Regulation on Insolvency Proceedings, Council Regulation (EC) No 1346/2000 of 29 May 2000, OJ L160/1, June 30, 2000.

rent or payments under mortgages or credit card loans. However, a charge over any form of receivable is within the scheme.

### **Regulation 3            Other companies**

Charges created by a company registered outside Great Britain over assets in England and Wales will come within the scheme whether or not the company has a branch or a place of business in England and Wales. Such charges will need to be registered in order to be effective in insolvency (unless exempted from registration). Similarly, their priority as against other security and as against a person who buys the property subject to the charge will be governed by the scheme. There will be special provisions for goods that are subject to a charge when they are brought into England and Wales (regulation 21). However, to reduce the uncertainty over aircraft and ships that are likely to move in and out of the country frequently, special rules apply to registered aircraft and registered ships. They will be regarded as situated in England and Wales if they are registered in the UK, and as not situated here if they are registered abroad, regardless of their physical location.

Implementation of the recommendations of the Scottish Law Commission in its Report on Registration of Rights in Security by Companies (Scot Law Com No 197, 2004) will mean that, in order to constitute a floating charge under Scots law, it will be necessary to register the text of the deed in a Register of Floating Charges. There will no longer be a requirement to register any security created by a company registered in Scotland with the Registrar of Companies. Under regulation 3, to enable those dealing with the company's assets in England and Wales to discover whether the assets are subject to a charge, the charge will be registrable in the same way as a charge created by a company registered outside Great Britain.

The provisions on sales of receivables do not apply to a company registered outside England and Wales, whether or not the company has registered a branch or place of business in Great Britain.

### **Regulation 4            Exceptions**

With the introduction of electronic conveyancing, it will become unnecessary for registered charges over registered land to be registered also at Companies House. The Land Registry already has the power to forward information about such charges to Companies House. Under the scheme, information will be forwarded routinely and made be available to those searching the Company Security Register. The scheme applies to such charges only to the extent that it deals with competing priorities between these and other charges over the land (regulation 25).

Liens and charges created by operation of law (regulation 4(1)(a)) are also outside the scheme, save that their priority as against other charges is dealt with by regulation 31.

The scheme contains a special exemption for Lloyd's Trust Deeds (see regulation 4(1)(g)). When a corporate member joins Lloyd's it is obliged to enter into several categories of trust deed to ensure that funds are available to pay policy-holders, and these are currently registrable as charges although most of the registrations serve little useful purpose.

Under the Regulations, the "Lloyd's Deposit Trust Deed" or "Lloyd's Security and Trust Deed" created by each corporate member will continue to be registrable. This will serve as a warning to all concerned that the company is a corporate member of Lloyd's and will probably have entered other trust deeds. Other trusts deeds will cease to be registrable. Charges other than trust deeds created by corporate members will need to be registered in the normal way.

Regulation 4(1)(b)-(e) exempt from the scheme various types of sale of receivable that are not connected to receivables financing.

## **PART 2                      FILING AND REGISTRATION**

### **Regulation 5 The Register**

Regulation 5, with the remainder of Part 2, sets up a register for company charges and sales of receivables that can be wholly electronic. Part 2 will be supplemented by Rules to be made by the Registrar under powers to be conferred by the Companies Bill.

Registration will be effected by 'filing' a 'financing statement'. The way that this will work is described below.

### **Regulation 6              Financing statement**

It is envisaged that the Rules will require a person wishing to register a charge or sale of receivables (who will normally be the chargee or buyer, or its agent) to contact Companies House to be authorised to use the system, if it has not done so before. (This may involve, for example, setting up payment arrangements and giving an email address that the Registrar may use for communicating with the party.)

The person will then 'file' a 'financing statement' on-line (either via the Company Security Register's website or under direct arrangements made by the Registrar and the filing party). The financing statement must contain information in each of the fields listed in regulation 6(2) and the confirmation required by regulation 5(3) must be given. It is envisaged that the system will provide an automatic check that both the name of the debtor and its registered number are given and that they match each other. If they do not, or if no number is given, the filing will not be accepted until the party filing either enters a matching name

and number or confirms that the company is an overseas company that has not registered a branch or place of business in Great Britain.

Once this is done and arrangements have been made for payment of the fees, the system will accept the filing. The date and time will be recorded on the financing statement and it will be given a number. From that moment, the financing statement will be 'registered' (regulation 7(1)). Subject to regulation 9, the charge or sale will then be registered unless the registration ceases to be effective because it was for a limited period that has expired or because it has been discharged.

A filing may be made before the charge agreement or sale agreement has been made. This enables a financier engaged in negotiations with the company to protect its priority. It also makes it unnecessary to file more than once for repeated transactions with the same company over similar collateral. This is important in receivables financing, where there may be many separate sales under a single agreement that does not itself constitute a sale.

A party filing will be required to confirm that either there is a charge or sale agreement or the company has consented to the filing. An incorrect confirmation will expose the filing party to liability in damages to the company for any loss it suffers as a result, unless the party filing can show that it had a reasonable excuse for its mistake. A filing made without an honest belief that there is an agreement or that the company has consented to the filing will lead to criminal liability under general provisions envisaged in the Companies Bill. The company named as debtor will be able to secure the removal of any incorrectly-made filing under regulation 16.

#### **Regulation 7            When registration is effective**

The financing statement is registered at the moment that the system assigns a number to it; the date and time will also be recorded. The date, time and (if necessary) the number will often determine questions of priority (for example, regulation 24).

#### **Regulation 8            Verification statement**

Once the financing statement has been registered, a verification statement will be sent to the person filing at the address given, and to the company identified as the debtor in the financing statement. In the case of a company registered in Great Britain or that has registered a branch or place of business in Great Britain, the 'verification statement' will be sent by the Registrar, either by email or by post, to the company's registered address (or such other address as the company may have provided for the purpose). In the case of other companies, the party filing will be obliged to send a copy of the verification statement to

the company, and will be liable in damages to the company for any failure to do so (regulation 17(2)).

### **Regulation 9            Errors in financing statement**

The system will check that the name and number given for the debtor company match (see above). However, it will not check the accuracy of any other information on the financing statement. If the financing statement has identified the wrong company, it will not be effective to register the charge or sale of receivables. This is because a search using the correct name and number would not reveal it.

With oversea companies that have not registered a branch or place of business in Great Britain, it is envisaged that those searching the register will be able to ask for 'near misses'. A registered financing statement that gave an incorrect name will be effective to register the charge unless a search using the 'near miss' facility would not have revealed the financing statement.

A mistake in the other fields will not invalidate the registration save that the charge will not be effectively registered in respect of collateral that was omitted from the description of the collateral.

### **Regulation 10          Additional statements**

Subsequent changes to a financing statement (such as to add or delete collateral or to discharge it altogether) will be made by filing an 'additional statement'. This will have to contain the number allocated to the financing statement that is being amended. A search will then reveal not just the original statement but any additional statements that have amended it. It is assumed that, after a while, discharged financing statements will be removed to an 'archive' file so that a search will not reveal them unless the searcher specifically asks for 'archived' material.

It is envisaged that the party who files will be issued with a personal identification number that will enable it to access the system to file additional statements. Where a party attempts to extend the period of registration or add to the security, it will be asked to confirm that this is in accordance with an existing security agreement or that the debtor has consented to the change. The sanctions will be as described under regulation 6, above.

In certain circumstances the debtor will also be able to effect changes by means of an additional statement (regulation 16).

### **Regulation 11          Extension or discharge of registration**

Registration of a financing statement that was limited to run only until a particular date may be extended by the party who filed by means of an additional statement.

## **Regulation 12      Amendment of financing statement**

See regulation 10, above.

## **Regulation 13      Notice of transfer**

Where a charge is assigned by the chargee to another person, it is not necessary to file an additional statement. However, it may be convenient for all concerned that the new assignee is recorded as the chargee so that enquiries and notices are sent direct to it. The same is true if the benefit of an agreement to sell receivables is assigned, for example by one factor to another. It is therefore provided that the transfer may be recorded.

## **Regulation 14      Notice of subordination**

The same is provided where the parties enter a subordination agreement.

## **Regulation 15      Searches**

Regulation 15 provides for searches, including the criteria by which searching must be made possible. For the significance of this see regulation 9, above.

## **Regulation 16      Debtor etc may require additional statement**

If the information shown in a registered financing statement is inaccurate (for example it refers to collateral not covered by the charge agreement), the debtor may demand that it be corrected. Similarly if the secured obligations have been discharged, the debtor may demand that the financing statement be discharged. If the company shown as the debtor has not entered a charge agreement with the person who is named as the chargee, or on whose behalf the financing statement was filed, it can demand that the registration be removed. Where the person was incorrectly identified as one of several debtors, the person wrongly identified can have its name removed, leaving in place the registration against other parties who were correctly named as debtors.

It is envisaged that in most cases the debtor will make its demand by entering on the system a 'requirement' notice, setting out what change is required. This will be sent to the party shown as chargee, or its agent, on the financing statement at the address shown. Within 15 days the recipient must either file a additional statement in accordance with the requirement notice or commence court proceedings and notify the Registrar that it has done so. Failing that, the debtor will be empowered to make the change demanded in the requirement notice. If proceedings have been commenced, the Registrar will mark the financing statement as contested. The financing statement will remain

registered until either the Registrar is notified of the court's order or the proceedings are dismissed or discontinued.

Where the chargee is merely a trustee for others (for example, for a group of lenders), the procedure will not apply, because an oversight by the trustee might lead to the beneficiaries losing their security through no fault of their own. If the financing statement indicates that the chargee is a trustee (which will be optional), the person named as debtor will need to obtain a court order to have the financing statement amended or discharged.

**Regulation 17 Entitlement to damages for incorrect filing, etc**

If a financing statement has been filed when there is no relevant agreement or the debtor has not consented to the filing, and the party filing had no reasonable excuse, the party who filed will be liable in damages to the company identified as the debtor.

A party who files a financing statement against a company that is not registered, and has not registered a branch or place of business in Great Britain, must forward the verification statement to the company (regulation 8). If it fails to do so without a reasonable excuse it will be liable in damages to the company.

**Regulation 18 Requirement to notify Registrar about appointment of a receiver**

This provision replicates the effect of the Companies Act 1985, section 405.

**Regulation 19 Filing is not notice**

Some provisions (regulations 21, 24, 28, 29, 35 and 38) refer to whether a party knew of a fact. Regulation 19 has the effect that registration of a financing statement does not give anyone 'constructive' notice of the existence of any charge to which it refers, or of the contents of the financing statement. Under the regulations, the priority of a registered charge against another registered charge or a pledge, for example, generally depends on the date of registration. Its effect against a buyer depends on whether it was registered and on the buyer's knowledge. In neither case does the outcome depend on 'constructive notice' of what has been registered.

**PART 3 EFFECTIVENESS OF CHARGES, ETC**

**Regulation 20 Effectiveness of a charge or a sale of receivables in insolvency proceedings**

Unless a charge is exempt from registration, it will not be effective against the company's administrator or liquidator unless it has been

registered before the onset of insolvency (regulation 20(1)). The charge will also be ineffective as against execution creditors (regulation 20(4)). (It will also be at risk of loss of priority to subsequent charges and pledges and ineffective against a buyer who does not know of it, see regulations 24 and 28. On charges that are registered in the 'run-up to insolvency', see regulation 45.)

A charge of any description and over any type of property falls within this regulation unless specifically exempted. The principal exemptions are for charges over:

financial collateral of which the chargee has 'control' (see regulation 36);

registered land that have been registered at the Land Registry (see regulation 4); and

'supporting obligations' such as guarantees and letters of credit, which will be treated as if they are registered when the charge over the principal obligation has been registered.

If as the result of the debtor company disposing of the collateral the chargee becomes entitled to the proceeds of disposition, its rights to the proceeds will be effective without separate registration (unless its right arises only because of the terms of a floating charge). The same applies if the collateral is damaged or destroyed and the chargee is entitled to the insurance proceeds (regulation 20(1)(c)).

The scheme extends the same treatment to sales of receivables. (For the definition of receivables see regulation 2.) There is one exception, to guard against accidental oversight by those not regularly engaged in receivables financing. Under regulation 20(2) it is not necessary to register a sale of receivables that is of such a small proportion of the company's receivables that its sale will not be significant to the decision of a subsequent receivables financier or unsecured creditor as to the extent of funds or credit that should be advanced to the company.

### **Regulation 21 Charges over imported goods**

Under regulation 3, charges created by Scottish and overseas companies over their assets in England and Wales will be subject to the scheme. When goods that are subject to a charge are brought into the jurisdiction, the charge will need to be registered if they remain here for more than 60 days. Otherwise it will be ineffective in the Scottish or overseas company's insolvency. Until the charge has been registered, it will be vulnerable to loss of priority and will be ineffective against a buyer who does not know of it (regulations 24 and 28). Special treatment is accorded to registered aircraft and registered ships (regulation 3).

## **Regulation 22      Pledge treated as charge if collateral made available to debtor**

Although generally a pledge requires that the pledgee retain possession of the pledged property, it has been held that if the property is released to the debtor under a 'trust receipt' or similar arrangement (for instance to allow the debtor to sell the property) the pledge continues. The pledgee is also entitled to the proceeds of any disposition of the property. Regulation 22 treats such arrangements as a charge which, if it is to be effective in the debtor company's insolvency, must be registered within 15 days (unless the property is returned to the pledgee within that time). Until the charge has been registered (which may be done in advance of the arrangement, see regulation 6), a buyer who does not know of it will take free of it (regulation 28) and it will be vulnerable to loss of priority (see regulation 24).

## **Regulation 23      Attornment by debtor**

A pledgee may take 'possession' of property that is in the physical possession or custody of a third person (for example, a warehousing company) if the third person agrees with the pledgee to hold to its order ('attorns' to the pledgee). There is authority that there may be a pledge where the debtor itself has physical possession or custody and attorns to the pledgee. (If the arrangement is in writing it is registrable as a bill of sale.) The arrangement may mislead others dealing with the debtor into believing that the property in the debtor's possession is unencumbered and under these Regulations it is treated as a charge.

## **PART 4                  PRIORITY**

### **Priority rules**

## **Regulation 24      Residual rules**

Regulation 24 sets out the rules that govern priority between charges and pledges over property other than financial collateral (regulation 36) and sums due under letters of credit (regulation 26). The rules also apply to the priority of sales of receivables. The fundamental principles are that priority of a charge or a sale of receivables dates from the date of registration of a financing statement covering the charge or sale. This may be before the charge has been created or the sale has taken place (regulation 6). The priority of a pledge dates from when it was created, which requires that the pledgee has possession (regulations 22 and 23). For this purpose, a contractual lien is considered to be a pledge (regulation 42). Charges over supporting obligations that have not been registered separately will have the same priority as the charge over the principal obligation.

The priority of a charge will apply to all advances made under the charge, including those made after the chargee has notice of a subsequent charge. This is not confined to advances that the chargee is under an obligation to make. However advances made without any obligation to do so after the chargee has notice of the interests of an execution creditor will not have priority over the interests of the execution creditor (regulation 24(11)).

Priority from date of registration of the financing statement will apply to floating charges as well as fixed charges, so that it will no longer be necessary to employ negative pledge clauses to protect the priority of a floating charge. Consequential amendments will be made to Insolvency Act 1986 to clarify the effect on preferential creditors and the fund for unsecured creditors (see regulation 45).

### **Regulation 25      Conflict with transactions registered in specialist registers**

Charges over certain types of asset may be registered in specialist registers. These include:

registered aircraft

registered ships

unregistered land (for registered land, see below)

patents

registered designs

registered trademarks.

Registration in the specialist register is not required to preserve the effectiveness of the charge in the debtor company's insolvency. However, it may be needed to create a legal mortgage or to preserve the priority of an equitable mortgage or charge against a subsequent purchaser or chargee. In these cases, the charge will also have to be registered in the Company Security Register if it is to be effective in the debtor company's insolvency. Regulation 25 provides that the priority of charges over such assets will be governed by any rules set out in the relevant enactment rather than by the date of registration in the Company Security Register.

Regulation 25 applies the same rule to charges over registered land registered in the Land Register, which do not require registration in the Company Security Register (regulation 4).

In some cases the enactment establishing the specialist registry does not lay down rules governing the priority of charges registered in it but leaves it to general law. For example, the priority of equitable charges over registered land is not affected by registration at the Land Registry. Here the rules of the Company Security Regulations will apply. Thus as between two equitable charges over registered land, if neither charge

is registered at the Land Register, priority will depend on which financing statement was first registered in the Company Security Register. If one is covered by a financing statement registered in the Company Security Register and the other is registered in the Land Register, priority will depend on which registration took place first.

### **Regulation 26      Sums due under letters of credit**

A charge may be taken over an obligation that is supported by a letter of credit. The chargee has an implied right to the sums due under the letter of credit and the scheme provides that the charge over these need not be registered separately from the charge over the principal obligation. Under regulation 24 above, the charge over the supporting obligation will have the same priority as that over the principal obligation. However it is possible that the principal obligation may be subject to competing charges (probably by accident, for example if the company assigns a particular receivable forgetting that it is already the subject of a general charge over receivables, or vice versa). In this rather particular context, regulation 26 provides that the chargee who notifies the issuing bank or the confirming bank (a 'nominated person') will have priority over one who has relied merely on registering the charge. The bank will normally have to pay the sum due to the party that first notified it; regulation 26 ensures that this will be the party who has priority.

### Transfers

### **Regulation 27      Priority of charges in transferred collateral**

If a company acquires property that is subject to a charge, that charge will still be effective though it is not registered against the name of the acquiring company (provided that, if the charge was originally created by another company, the charge was registered against that company). Regulation 27 ensures that the charge will have priority over any charge that already exists, or that is created later, over the property of the acquiring company. (There is in effect an exception in those cases related to financial collateral in which the chargee's interests may be overridden in order to preserve the ready transferability of financial collateral, see regulation 38).

### **Regulation 28      Transfer of collateral free of unregistered charge**

A purchaser of property that is subject to a charge (other than a purchaser by way of security and a buyer of receivables: see regulation 28(5)(b) and regulation 24 above) will take free of an unregistered charge unless the purchaser knows of the charge. If the charge is a floating charge, the purchaser will take free unless it also knows that disposition is in breach of the charge (regulation 28(3)), and the same rule is applied to transferees of negotiable instruments and negotiable

documents of title in order to maintain their ready transferability (regulation 28(2)).

**Regulation 29            Circumstances in which transferee takes collateral free of registered charge**

A buyer of the property subject to a registered charge will take subject to the charge unless the disposition is specifically authorised or the charge is a floating charge. The buyer of property subject only to a floating charge will take free unless it knows that the sale is in breach of the charge. In practice this will rarely happen unless a receiver has been appointed or the company has ceased trading or is in administration or liquidation.

Regulation 29 applies to a charge that was created as a floating charge. There is some uncertainty over what happens if a chargee takes a fixed charge and then permits the chargor to dispose of the property without obtaining consent on each occasion. This may make the fixed charge wholly ineffective or it may transform it into a floating charge. Regulation 29(2)(b) covers the latter possibility.

**Regulation 30            Protection of transferees of money, negotiable instruments etc**

This saving provision preserves the protection the law currently provides to recipients of money and funds transfers, holders in due course of negotiable instruments and holders of negotiable documents of title.

Miscellaneous

**Regulation 31            Priority: liens**

This preserves the current rule that a lien or charge that arises by operation of law has priority over a charge over the same property.

**Regulation 32            Distress for rent or rates**

Regulation 32(1) preserves the priority of a landlord's right to distrain on goods over a charge on the same goods. Regulation 32(2) provides that a local authority's rights to distrain on goods for unpaid rates will be subject to a registered charge. Under current law the local authority is in principle entitled to distrain if the charge is a floating charge that has not crystallised. In practice the floating charge will normally include an 'automatic crystallisation clause', causing the charge to crystallise as soon as any attempt is made to distrain. Such clauses defeat the local authority's right. Thus this Regulation reflects the practical position.

**Regulation 33            Effect on priority of mistaken discharge of filing**

It is possible that a registered financing statement may be discharged by accident, either by the secured party or by an agent acting for it. That will have the result that the charge will not be effective in insolvency or affect a buyer. It will also lose priority to any subsequently registered charge. However, if the mistake is picked up and corrected within a short period, it seems hard that the chargee should lose its priority even against charges that, before the discharge, were subordinate to it. Those chargees are very unlikely to have acted in reliance on the discharge. Therefore regulation 33 provides a 30-day grace period in which the discharged filing can be re-activated (by means of a further additional statement) without loss of priority as against the previously subordinate charges.

### **Regulation 34      Voluntary subordination**

The purpose of regulation 34 is to make it clear that it is always possible for a chargee to subordinate its rights to what would otherwise be a junior charge (or sale of receivables). This may be done, for example, by an agreement between the senior and junior creditors; or the charge agreement may permit the creation of charges that will rank above it in priority.

Consequential amendments will be made to Insolvency Act 1986 to clarify the effect of a subordination agreement on preferential creditors and the fund for unsecured creditors. See the notes to regulation 45.

### **Regulation 35      Rights of assignees**

Regulation 35(1)-(4) ensure that the new rules of priority do not affect the existing law

- (1) on when an account debtor may, as against an assignee, rely on defences and set-offs that it has against the assignor; and
- (2) that a debtor who pays the assignor before it has received notice of the assignment will discharge its obligation by doing so, but after receiving notice of assignment must pay the assignee.

Regulation 35(5) applies to contracts that create receivables, defined narrowly to cover only those debts commonly subject to factoring or discounting agreements. The regulation provides that a term in the contract purporting to prohibit or restrict assignment of the receivable (other than an assignment in part) will not be effective against the assignee. This removes a common (but often unintentional) obstacle to receivables financing.

## **PART 5                      FINANCIAL COLLATERAL**

This Part applies only to financial collateral, which needs separate treatment in order:

- (1) to comply with the requirements of the European Directive on Financial Collateral Arrangements<sup>36</sup> ('the Financial Collateral Directive' or 'FCD') and the Financial Collateral Arrangements (No 2) Regulations 2003<sup>37</sup> ('FCAR') which implement the FCD, and
- (2) to ensure that investment property is freely transferable without the need for the purchaser (whether intending buyer or secured party) to make investigations as to whether the property is subject to a charge.

The provisions on financial collateral apply to 'investment property' and to 'cash'. Regulation 41 defines 'investment property' as

- (3) 'financial instruments', whether these are securities for which there is a certificate ('certificated financial instruments') in bearer form or registered form, or are uncertificated. The definition of 'financial instruments' is closely modelled on that used in the FCAR, but is limited to directly-held interests; and
- (4) any other form of 'financial asset' that is held through an intermediary. This includes rights under commodity futures contracts and options. The account to which to which financial assets may be credited or debited is termed a 'securities account', the person who maintains the account as an 'intermediary' and the person in whose name the intermediary maintains the account as the 'account holder.'

'Cash' has a particular meaning that is found in the FCD and the FCAR. It means not cash in the everyday sense ('money') but sums of money credited to an account (including a bank account), money market deposits and sums due under a close-out netting arrangement.

In outline, the FCD provides that when financial collateral subject to a 'security financial collateral arrangement' (that is, a mortgage, charge or pledge) has been 'provided' in such a way as to be in the 'possession or control' of the 'collateral-taker', formalities such as registration cannot be required in order to render the arrangement enforceable (art 3).

(The FCD also requires that certain remedies must be available (unless otherwise agreed) and remain so notwithstanding winding-up or re-organisation of either party (art 4); that agreed rights of use must be available (art 5); and the arrangements must be exempted from certain effects of insolvency law (art 8). These aspects of the FCD are not affected by the Company Security Regulations. Nor are 'title-transfer collateral arrangements', such as 'repos', to which the FCD also applies.)

The FCD does not define what is meant by 'possession or control', and it does not deal with the priority of security interests over financial

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<sup>36</sup> Directive 2002/47/EC of the European Parliament and Council of 6 June 2002, OJ L 168/43.  
<sup>37</sup> SI 2003 No 3226.

collateral or the rights of buyers. The Company Security Regulations provide guidance as to when charges over financial collateral need not be registered. They also set out rules of priority as between competing charges and other forms of security, and as between a security interest and the interest of a person who purchases the financial collateral not knowing of a charge over it.

**Regulation 36      Effectiveness of charges over investment property or cash in insolvency proceedings**

Like charges over other forms of collateral, a charge over financial collateral will be effective in the debtor company's insolvency if it is registered. However, as an alternative to registration the chargee may take control of the financial collateral. Not only will taking control render the charge effective in the company's insolvency; it will confer advantages in terms of priority.

The FCAR do not provide a definition of 'possession or control'. The recitals to the Directive indicate that the chargee will not have 'possession or control' if the debtor company remains free to dispose of the collateral free of the charge. It is widely agreed that if the debtor company is no longer free to dispose of the collateral free of the charge (often described as the chargee having 'negative control'), that amounts to 'possession or control' within the FCD. The Law Commission is as confident as it can be that this is the correct test to apply. However it is advised that it cannot rule out the possibility of the European Court of Justice adopting a more liberal interpretation. For example, the ECJ might hold that a party has 'possession or control' if it is in a position to realise the company's investment property at short notice, even though the debtor meanwhile remains free to deal with the collateral. (In English law this would amount to a form of floating charge.) It has therefore proved impossible to provide a definition for the purposes of the Directive without the risk that parties to arrangements that relied on the definition might be deprived of the rights (for example, in insolvency proceedings) that they must be given under the FCD. Conversely, they might receive preferential treatment that is not justifiable under the Directive.

Nonetheless, the Regulations give guidance on when a charge need not be registered. They provide that it need not be registered when either the chargee has 'possession or control' within the meaning of the FCD (whatever that means) or it has control within the meaning set out in detail in regulation 40. A chargee who obtains control within the terms of regulation 40 can be confident that the charge will not be ineffective in insolvency for want of registration. It is also widely agreed that the chargee who complies with regulation 40 or 41 will have done sufficient to have 'possession or control' within the meaning of the FCAR and thus to gain the various advantages offered by the FCD. It is possible that a party who has merely taken steps that do not meet the tests set out in regulation 40 may also be held to have satisfied the

requirements of the FCD. It would then be entitled to the same advantages, including its charge being effective in the debtor's insolvency though not registered. Whether a chargee wishes to take the chance that a more liberal interpretation of the FCD is correct is a matter for its legal and commercial judgement.

The test of 'control' laid down in regulation 40 is also used to determine issues of priority under regulation 39.

### **Regulation 37      Automatic charge in favour of intermediary etc**

It may happen that an investor buys indirectly-held financial assets through an intermediary, which credits them to the investor's account before the investor has paid the intermediary. The intermediary will have an automatic fixed charge over the assets. The charge does not require registration to be effective but it will lose priority to a subsequent charge under which the chargee takes control of the collateral (regulation 39). A charge will also arise in favour of a party who delivers certificated financial instruments under an agreement under which payment was due on delivery before the payment has been made, but in this case, since the relevant certificate has been handed over to the debtor, the charge will be only a floating charge.

### **Regulation 38      Purchaser takes free: investment property**

Regulation 38 sets out rules on when purchasers of investment property will take free of a charge over the property. The provisions are designed to ensure that investment property is readily transferable without the need for purchasers to make enquiries. Essentially, purchasers who do not know of the security interest, or know of it but do not know that the disposition to them is in breach of the security agreement, will take free if (before they acquire any relevant knowledge) they take the investment property into their own name. A person does not have knowledge of something for the purposes of the scheme merely because it has been included in a registered financing statement (Regulation 19). Thus 'innocent' purchasers who have taken the steps described can be confident that no other charge over the investment property will be effective against them.

Under the regulations, 'purchaser' includes a mortgagee or chargee. This means that a secured creditor may rely on regulation 38 even when it would not obtain priority under regulation 39. Thus if a secured creditor is permitted to have investment property transferred into its name, not knowing that the disposition to him is in breach of a previous charge agreement, it will take free of the charge. This will apply if the previous charge was a floating charge, or if it was a fixed charge which was merely registered instead of the chargee having control of the collateral. It will also apply if the chargee under the previous charge had obtained control but by some accident the collateral was nonetheless transferred into the name of the second secured creditor.

This might happen if, for example, an intermediary overlooked a notice of assignment or an agreement with the earlier chargee. The earlier chargee would have a remedy against the intermediary but the second secured party would take free.

### **Regulation 39      Special priority rules for investment property and cash**

Regulation 39 sets out the rules governing the priority of competing charges and, for the rare cases where it will be relevant, pledges of financial collateral. The basic principles are two. First, a charge perfected by control will take priority over one that is not perfected by control, for example, one that is perfected by registration (and see regulation 37). This means that a chargee who has control may safely advance funds without needing to search to see if a charge over the collateral has been registered. Secondly, as between competing charges each of which is perfected by control, priority depends on the order in which control was obtained. For directly-held securities, it is not possible for more than one secured party to obtain control. Where investment property is held through an intermediary and with cash, it is possible. In each case a potential chargee can make enquiries of the intermediary or 'cash debtor' to find whether any other party already has control.

Any issues not settled by regulation 39 fall to be decided according to the residual rules on priority in regulation 24.

It should be noted that a secured party may also be a protected purchaser within regulation 38. This may result in a mortgagee of investment property taking priority even over an earlier charge that has been perfected by control of another form, such as by notification of the charge to the intermediary.

### **Regulation 40      Meaning of control**

Regulation 40 sets out steps that a chargee (or, in the case of a bearer security, a pledgee) of particular forms of investment property may take to obtain control over various forms of investment property and over 'cash'.

In each case there must be evidence in writing of the agreement and the arrangement under which the collateral was provided, as required by the FCAR. However the requirement is attenuated. It need not be signed and it need only be available by the time the relevant dispute arises. Moreover, in accordance with the accepted interpretation of the FCD (based on the travaux préparatoires) a recording of a telephone or other conversation will suffice (as will an email or other electronic communication using writing, which is generally sufficient in English law to satisfy a requirement of writing).

Paragraph (2) deals with bearer securities, (3) with directly held-certificated registered shares and paragraph (4) with uncertificated securities held in the CREST system.

Paragraphs (5) and (6) deal with financial assets held through an intermediary, and paragraphs (7) and (8) with 'cash'. In the majority of cases the chargee can obtain control by giving notice of its interest to the intermediary or 'cash debtor' ('cash debtor' is defined in regulation 41(1)). If the intermediary or cash debtor is entitled to disregard a notice of assignment, the chargee will need to obtain that person's agreement in order to achieve control.

Regulation 40(9) provides a 'residual test' for cases that do not fall within (2)-(8), for example new situations that might emerge. It is, in broad terms, that the chargee will have control (within the meaning of these Regulations) if it has the 'negative control' described earlier. It too is subject to the requirement of evidence in writing, see above.

#### **Regulation 41            Meaning of other expressions used in Part 5**

So far as appropriate, the definitions and terms used in relation to financial collateral are the same, or are derived from, those in the FCD, the FCAR and the Hague Convention on the Law applicable to certain Rights in respect of Securities held with an Intermediary.

### **PART 6                    MISCELLANEOUS AND SUPPLEMENTARY**

#### **Regulation 42            Interpretation: General**

Regulation 42 provides definitions of a number of terms that are used in the Regulations and which are not defined in the particular regulation in which they appear.

#### **Regulation 43            Index of defined terms**

This index enables a user to find the definition of any of the terms defined in the Regulations.

#### **Regulation 44            Account debtors and cash debtors**

This Regulation is to confirm that a 'charge-back', or similar agreement under which a debtor takes a charge over the sum that it owes to the chargor, may be effective.

#### **Regulation 45            Consequential amendments**

This regulation will make a number of amendments to Insolvency Act 1986. [Items (2), (3) and (4) are yet to be drafted.]

- (1) Because it will be possible to register a financing statement at any time, section 245 of the Act will be amended to apply not only to

floating charges created in the run-up to insolvency but also to those created before the run-up yet only registered during that period.

- (2) Under the scheme, a floating charge that is registered before a subsequent fixed charge will have priority over the fixed charge, unless the parties agree otherwise. However, in insolvency preferential creditors and the unsecured creditors' fund have priority over the floating charge but not the fixed charge. (The same issue arises under current law if the fixed chargee takes with notice of a negative pledge clause in the floating charge.) An amendment to the Act will provide that as, against the preferential creditors and the unsecured fund, the floating charge should have priority to the extent of any fixed charges over which it has priority.
- (3) In practice, where a person contemplating taking a fixed charge over a company's assets discovers that the company has already granted a floating charge over the same assets, it will normally not go ahead without reaching an agreement with the floating-charge-holder. It will seek to obtain the fixed charge-holder's agreement to allow the fixed charge to take priority. (This is frequently done under current law if the person suspects the floating charge may contain a negative pledge clause.) A further amendment to the Act will make it clear that such a subordination agreement, or any other arrangement that a fixed charge should have priority to a floating charge, will result in the fixed charge also having priority over the preferential creditors and the unsecured fund.
- (4) Payments may be made to a secured creditor and the relevant financing statement then discharged, but later the payments may be 'clawed back' by the liquidator under the provisions of the Act. Provision will be made, if necessary, to ensure that the creditor's right to revert to the security is not impaired.

#### **Regulation 46      Transitional provisions and savings**

It will not be necessary to re-register charges that were registered before the date of commencement of the new scheme. They will remain effective and retain their priority as against other pre-commencement charges. As against post-commencement interests, they will be treated as having been registered at the moment of commencement, thus normally giving them priority against later interests (other than charges perfected by control).

Equally it will not be necessary to register charges that were created before the commencement but under current law do not require registration. (This is because it would be very difficult and expensive for many chargees to identify all the unregistrable charges they hold.) These will therefore not appear on the register; it is envisaged that the system will carry a warning of this to searchers. They too will remain

effective and retain their priority as against other pre-commencement charges; and they will be treated as having been registered at the moment of commencement.

In contrast, by the end of a transitional period of 2 years sales of receivables and arrangements under which receivables may be sold must be covered by a financing statement. (Such agreements will be much easier to identify, since the agreement will normally be 'active', with receivables being transferred and payments made by the receivables financier to the company on a regular basis.)

## **ANNEX C.1 List of Recommendations made by the Scottish Law Commission**

1. Constitution of a floating charge, as an inchoate security right, should take place on registration.
2. There should be a register of floating charges in which all floating charges must be registered, irrespective whether the grantor is a company registered in Scotland or has registered a branch or place of business with the Registrar of Companies.
3. The Register of Floating Charges should be maintained by the Keeper of the Registers of Scotland.
4. The text of the deed of floating charge itself should be registered in the Register of Floating Charges.
5. (a) A system of advance notices should be introduced for floating charges.  
(b) The registration of an advance notice should confer a priority period of up to 21 days in respect that, if presented within that period, the floating charge to which the notice relates is deemed to have been registered on the date of the advance notice.  
(c) An advance notice should be given jointly by or on behalf of both the grantor and the grantee of the intended floating charge.  
(d) An advance notice should not be renewable.
6. (a) Floating charges should rank with other securities, whether fixed or floating, by date of creation.  
(b) "Creation" for this purpose means –
  - i. in the case of a floating charge the date on which the floating charge document was registered or deemed to be registered and
  - ii. in any other case, the date on which the security was constituted as a real right.  
(c) The rule at (a) should be capable of being altered by a ranking agreement contained in the registered floating charge or a registered document of alteration
7. An assignation of a floating charge should vest the floating charge in the assignee only on registration of the assignation.
8. The terms of an instrument of floating charge should not be held amended by an instrument of alteration unless that instrument of alteration has itself been registered.
9. Property may be released from a floating charge only on registration of an instrument of alteration to that effect.

10. A floating charge may be discharged by registration of a deed of discharge.
11. The provisions which we propose regarding floating charges granted by companies should also apply to floating charges granted by limited liability partnerships; European economic interest groupings; and by industrial and provident societies.
12. Floating charges should cease to be registrable in the registers of patents, trademarks and registered designs respectively.
13. There should no longer be any requirement to register particulars of a security granted by a company with the Registrar of Companies.
14. There should no longer be any requirement to register with the Registrar of Companies particulars of a security granted by a limited liability partnership or a European economic interest grouping.
15. The existing duty of directors to deliver to the Registrar an annual return should be supplemented by a requirement to include in the annual return details of securities granted by the company, and not discharged, as at the return date.
16. The particulars to be contained in the company's securities return should be –
  - (a) a short description of the property over which the security is granted;
  - (b) the form of the security;
  - (c) the name of the grantee;
  - (d) the date upon which the security was granted; and
  - (e) the obligation for which security is given.
17. (a) A company should no longer be under any statutory duty to maintain an internal register of charges; but
  - (b) On being requested to do so, and on payment of such fee as may be prescribed, a company should be under a statutory duty to supply to the inquirer details of any security granted by the company since the return date of the last annual securities return being those details which would fall to be included in a securities return; or if no such security has been granted, to inform the inquirer accordingly.
18. (a) A company should be required to keep, at its registered office, a copy of every security deed granted by it and any deed altering or assigning the security.
  - (b) Copies of such security deeds should be open to general inspection on payment of such fee as may be prescribed.
19. No requirement, additional to registration in the Register of Floating Charges, should be imposed under the law of Scotland before a floating

charge may be effective to embrace, on crystallisation, assets located outside Scotland

20. A floating charge granted by an overseas incorporated company and intended to be effective in Scotland as respects assets located in Scotland should require to be registered in the Register of Floating Charges.
21. A floating charge granted by a company incorporated in England and Wales and intended to be effective in Scotland as respects assets located in Scotland should require to be registered in the Register of Floating Charges.

## **ANNEX C.2 Scottish Law Commission's Draft Legislative Provisions**

NOTE: These draft provisions assume that Chapter II of Part XII (registration of charges) and Part XVIII (floating charges) of the Companies Act 1985 have been repealed as part of a wider repeal of provisions of that Act – see paragraphs 1.22 and 1.23 of the report.

### **PART 1**

#### FLOATING CHARGES

##### **1 Creation of floating charges**

- (1) A company may, for the purpose of securing any debt or other obligation incurred or to be incurred by, or binding upon, the company or any other person, grant in favour of the creditor in the debt or obligation a charge (a "floating charge") over all or any part of the property which may from time to time be comprised in the company's property and undertaking.
- (2) On and after the coming into force of this section, a floating charge is (subject to section 2) created only when a document—
  - (a) granting a floating charge, and
  - (b) subscribed by the company granting the charge,is registered in the Register of Floating Charges.

#### NOTE

Subsection (1) derives from section 462(1) of the 1985 Act and restates the statutory rule that, in Scotland, a company may grant a floating charge. In view of the generality of the phrases "debt or other obligation" and "all or any part of the property" the reference in parentheses in the existing provision to the former including a "cautionary obligation" and the latter "uncalled capital" is unnecessary. The term "company" is defined in clause 13 of the draft Legislative Provisions. Subsection (2) implements Recommendation 1. It lays down the new rule that, after the proposed legislation enters into force, the creation of a floating charge occurs only when the document granting the floating charge is registered in the Register of Floating Charges (which is instituted in terms of clause 9). See paragraphs 2.2 – 2.5 of the report. Section 462(5) of the 1985 Act provides that a floating charge has effect in relation to heritable property without the need for the document granting the charge to be recorded in the Land Register or Register of Sasines. It is evident from section 28 of the Land Registration (Scotland) Act 1979 that a floating charge constitutes an "overriding interest" and is not a registrable interest. The provision that floating charges are created by registration in the Register of Floating Charges implies no further act of registration is required and the terms of section 462(5) are not re-enacted in these draft Legislative Provisions.

##### **2 Advance notice of floating charges**

- (1) Where a company proposes to grant a floating charge, the company and the person in whose favour the charge is to be granted may apply to have joint notice of the proposed charge registered in the Register of Floating Charges.
- (2) A notice under subsection (1) must—
  - (a) be in such form,
  - (b) contain such particulars, and
  - (c) be given in such manner,

as the Secretary of State may by order made by statutory instrument prescribe.

- (3) Where—
  - (a) a notice under subsection (1) is registered in the Register of Floating Charges, and
  - (b) within 21 days of the notice being so registered, a document—
    - (i) granting a floating charge conforming with the particulars contained in the notice, and
    - (ii) subscribed by the company granting the charge,is registered in the Register of Floating Charges,

the floating charge so created is to be treated as having been created when the notice was so registered.
- (4) An instrument containing an order under subsection (2) is subject to annulment in pursuance of a resolution of either House of Parliament.

**NOTE**

This clause implements Recommendation 5 by making provision for the registering of an advance notice of a floating charge. See paragraphs 2.12 – 2.15 of the report. The purpose of an advance notice is to assist the mechanics of settling secured transactions by allowing parties to obtain priority of ranking from the date of the advance notice provided that settlement is completed to the extent that the floating charge is registered within 21 days of the advance notice. An advance notice cannot be registered unilaterally. The form of an advance notice and the way in which it may be given may be prescribed by statutory instrument. It is envisaged that the regulations may provide that the advance notice may be subscribed either by the parties or by their solicitors.

**3 Ranking of floating charges**

- (1) Subject to subsections (2) to (4) and to any provision made under subsection (5), a floating charge, created on or after the coming into force of this section, which has attached to all or any part of the property of a company—
  - (a) ranks with—
    - (i) any other floating charge which has attached to that property or any part of it, or
    - (ii) any fixed security over that property or any part of it, according to date of creation, and
  - (b) ranks equally with any floating charge or fixed security referred to in paragraph (a) which was created on the same date as it was created.
- (2) Where all or any part of the property of a company is subject to both—
  - (a) a floating charge, and
  - (b) a fixed security arising by operation of law,the fixed security has priority over the floating charge.
- (3) Where the holder of a floating charge over all or any part of the property of a company has received intimation in writing of the subsequent creation of—
  - (a) another floating charge over the same property or any part of it, or
  - (b) a fixed security over the same property or any part of it,

the priority of ranking of the first-mentioned charge is restricted to security for the matters referred to in subsection (4).

- (4) Those matters are—
  - (a) the present debt incurred (whenever payable),
  - (b) any future debt which, under the contract to which the charge relates, the holder is required to allow the debtor to incur,
  - (c) any interest due or to become due on the debts referred to in paragraphs (a) and (b),
  - (d) any expenses or outlays which may be reasonably incurred by the holder, and
  - (e) in the case of a floating charge to secure a contingent liability (other than a liability arising under any further debts incurred from time to time), the maximum sum to which the contingent liability is capable of amounting, whether or not it is contractually limited.
- (5) The document granting a floating charge over all or any part of the property of a company may make provision regulating the order in which the charge ranks with any other floating charge or any fixed security (including a future floating charge or fixed security) over that property or any part of it.
- (6) Where provision is made under subsection (5), the document granting the charge requires to be subscribed by the holder of any subsisting floating charge, or any subsisting fixed security, which would be adversely affected by the provision.
- (7) For the purposes of subsection (1)—
  - (a) the date of creation of a fixed security is the date on which the right to the security was constituted as a real right, and
  - (b) the date of creation of a floating charge subsisting before the coming into force of this section is the date on which the instrument creating the charge was executed by the company granting the charge.
- (8) This section is subject to sections 175 and 176 (preferential debts in winding up) of the Insolvency Act 1986.

#### NOTE

This clause is concerned with the ranking of a floating charge both with other floating charges and with fixed securities affecting all or part of the same property as that covered by the floating charge. Subsection (1) sets out the leading principle that ranking proceeds on the basis of date of creation which, in the case of fixed securities is the date upon which the security was constituted as a real right (see subsection (7)). It implements Recommendation 6. See paragraphs 2.16 – 2.19 of the report. Where the floating charge is created on the same day as another floating charge or fixed security, the rule is that the respective securities rank equally. Subsection (2) is concerned with a competition between a floating charge and a fixed security arising by operation of law – such as lien or a landlord's hypothec. It continues the existing rule that such fixed securities arising by operation of law have priority over any floating charge. Subsection (3) continues an existing provision whereby the holder of the second, later floating charge may protect the value of his security by giving notice to the holder of the earlier floating charge in which event the priority ranking of the earlier floating charge is restricted to the amount of the debt then outstanding plus any further advances which the holder of that earlier floating charge is contractually obliged to make. In view of the change in the ranking rule, the same facility is extended to the holder of a subsequent fixed security. The ranking of securities may be the subject of agreement among the secured creditors and this is dealt with in subsections (5) and (6), the latter of which makes express what might otherwise be implied namely that any ranking agreement requires the participation of the holder of any subsisting security who would be adversely affected by

the ranking arrangement. Reference should be made to clause 6 for the method whereby a ranking agreement may be registered. The priority of preferential debts is preserved by subsection (8).

#### **4 Ranking of floating charges: transitional arrangements**

- (1) Floating charges subsisting immediately before the coming into force of this section rank with each other as they ranked with each other in accordance with section 464 of the Companies Act 1985 immediately before the repeal of that section by this Act.
- (2) A floating charge subsisting immediately before the coming into force of this section ranks with a fixed security so subsisting as it ranked with the security in accordance with section 464 of that Act immediately before the repeal of that section by this Act.
- (3) Despite the repeal by [*this Act*] of Chapter II of Part XII of that Act and Chapters I and III of Part XVIII of that Act, those provisions are to be treated as continuing in force in so far as is necessary for the purposes of subsections (1) and (2).

#### **NOTE**

The new rules on creation of floating charges and ranking by date of creation will not disturb the priority of ranking of existing securities, whether fixed or floating, since they have all been created prior to the coming into force of the new rules. Holders of such securities will not be adversely affected by the creation of any new floating charge. However, for clarity, this clause is intended to make plain that, for existing security rights, the existing rules continue in force.

#### **5 Assignment of floating charges**

- (1) A floating charge may be assigned (and the rights under it vested in the assignee) by the registration in the Register of Floating Charges of a document of assignment subscribed by the holder of the charge.
- (2) An assignment under subsection (1) may be in whole or to such extent as may be specified in the document of assignment.
- (3) This section is without prejudice to any other enactment, or any rule of law, by virtue of which a floating charge may be assigned.

#### **NOTE**

The existing legislation contains no provision on assignment of floating charges but in one first instance judicial decision (*Libertas – Kommerz v Johnson* 1977 SC 191) it was held that a floating charge was assignable on general principles of law. Subsection (1) gives statutory affirmation of the assignability of a floating charge and further gives effect to Recommendation 7 by providing for vesting in the assignee on registration in the Register of Floating Charges. Subsection (2) makes clear that partial assignment is possible. Subsection (3) is necessary since a floating charge may transfer not only by voluntary assignment but also by operation of law (eg on bankrupt sequestration of the holder the floating charge transfers to his trustee). See paragraph 2.20 of the report.

#### **6 Alteration of floating charges**

- (1) The terms of the document granting a floating charge may be altered, but only by a document of alteration—
  - (a) subscribed by—
    - (i) the company which granted the charge,
    - (ii) the holder of the charge, and

- (iii) the holder of any other subsisting floating charge, or any subsisting fixed security, which would be adversely affected by the alteration, and
  - (b) registered in the Register of Floating Charges.
- (2) But paragraph (a)(i) of subsection (1) does not apply in respect of an alteration which—
  - (a) relates only to the ranking of the first-mentioned charge with any other floating charge or any fixed security, and
  - (b) does not adversely affect the interests of the company which granted the charge.
- (3) The granting, by the holder of a floating charge, of consent to the release from the charge of any of the property to which the charge relates is to be treated as constituting an alteration to the terms of the document granting the charge.

**NOTE**

This clause implements Recommendations 8 and 9. See paragraphs 2.21 – 2.23 of the report. It is intended to ensure that third parties can rely upon the Register. Given that the terms of a floating charge must be published in the Register, it follows that any agreement between the holder of the floating charge and any other adversely affected security holder to alter the terms of the floating charge or its ranking must likewise be registered before it can receive effect as an alteration of the registered text. An unregistered agreement to alter the terms of a floating charge would remain as a contractual agreement between the parties to it but could not affect any third party.

One way in which the terms of a floating charge may be altered is by inserting a ranking agreement or changing an existing ranking arrangement. A ranking agreement is essentially an agreement between secured creditors and may be of no interest to the debtor. Subsection (2) enables an agreement between the secured creditors, in which the debtor is not participant, to be registered, provided that the debtor is not thereby adversely affected.

Subsection (3) addresses the case – exemplified in *Scottish & Newcastle plc v Ascot Inns Ltd* 1994 SLT 1140 - in which the holder of a floating charge gives his consent to specific assets, or a specific class of assets, of the company being released from the scope of the floating charge while yet remaining in the ownership of the company. If, as is currently the case, the fact of such a release is not published, an acquirer from a receiver appointed by the holder of the floating charge cannot be confident of his title. The subsection is not, of course, directed towards the escape of individual assets from the scope of the charge on the onerous or gratuitous transfer of the asset by the company to a third party prior to attachment of the floating charge.

**7 Discharge of floating charges**

- (1) A floating charge may be discharged by the registration in the Register of Floating Charges of a document of discharge subscribed by the holder of the charge.
- (2) A discharge under subsection (1) may be in whole or to such extent as may be specified in the document of discharge.
- (3) This section is without prejudice to any other means by which a floating charge may be discharged or extinguished.

**NOTE**

This clause implements Recommendation 10. It is essentially facultative. Payment of the debt, or performance of the obligation, secured by the floating charge will normally discharge or extinguish the security and this is recognised in subsection (3). But it is useful to have a means whereby the Register of Floating Charges may be cleared of floating charges which have been so discharged or extinguished. There may also be instances in which, as part of a re-financing arrangement, it is desired to discharge an existing floating charge in favour of

some other form of security and this clause provides a ready, public means of achieving that. See paragraphs 2.25 – 2.26 of the report.

## **8 Effect of floating charges on winding up**

- (1) Where a company goes into liquidation (within the meaning of section 247(2) of the Insolvency Act 1986), a floating charge created over property of the company attaches to the property to which it relates.
- (2) The attachment of a floating charge to property under subsection (1) is subject to the rights of any person who—
  - (a) has effectually executed diligence on the property to which the charge relates or any part of it,
  - (b) holds over that property or any part of it a fixed security ranking in priority to the floating charge, or
  - (c) holds over that property or any part of it another floating charge so ranking.
- (3) Interest accrues in respect of a floating charge which has attached to property until payment is made of any sum due under the charge.
- (4) Part IV (except section 185) of the Insolvency Act 1986 has (subject to subsection (1)) effect in relation to a floating charge as if the charge were a fixed security over the property to which it has attached in respect of the principal of the debt or obligation to which it relates and any interest due or to become due on it.
- (5) Subsections (1) to (4) do not affect the operation of—
  - (a) sections 53(7) and 54(6) (attachment of floating charge on appointment of receiver) of the Insolvency Act 1986, or
  - (b) sections 175 and 176 (payment of preferential debts in winding up) of that Act.

### **NOTE**

The essence of a floating charge is that until either the company goes into liquidation or a receiver is appointed the security right is inchoate and the company may dispose (even gratuitously) of assets within the scope of the charge and the acquirer will obtain ownership unencumbered by any security right. This clause, which simply repeats the existing law, deals with attachment, or crystallisation, of the floating charge on a winding up, when the floating charge is converted into a fixed security over the assets then within its scope. A floating charge similarly attaches or crystallises on the appointment of a receiver. The relevant statutory provisions on receivership are in the Insolvency Act 1986. They are not affected by the proposed reforms. Going into liquidation "within the meaning of section 247(2) of the Insolvency Act 1986" encompasses the insolvent liquidation of assets of an overseas company – see sections 220 and 221 of that Act.

## **9 Register of Floating Charges**

- (1) The Keeper of the Registers of Scotland (the "Keeper") must establish and maintain a register to be known as the Register of Floating Charges.
- (2) The Keeper must accept an application for registration of—
  - (a) any document delivered to the Keeper in pursuance of section 1, 5, 6 or 7, and
  - (b) any notice delivered to the Keeper in pursuance of section 2,

provided that the application is accompanied by such information as the Keeper may require for the purposes of the registration.

- (3) On receipt of such an application, the Keeper must note the date of receipt of the application; and, where the application is accepted by the Keeper, that date is to be treated for the purposes of this Part as the date of registration of the document or notice to which the application relates.
- (4) The Keeper must, after accepting such an application, complete registration by registering in the Register of Floating Charges the document or notice to which the application relates.
- (5) The Keeper must—
  - (a) make the Register of Floating Charges available for public inspection at all reasonable times,
  - (b) provide facilities for members of the public to obtain copies of the documents in the Register, and
  - (c) supply an extract of a document in the Register, certified as a true copy of the original, to any person requesting it.
- (6) An extract certified as mentioned in subsection (5)(c) is sufficient evidence of the original.
- (7) The Keeper may charge such fees—
  - (a) for registering a document or notice in the Register of Floating Charges, or
  - (b) in relation to anything done under subsection (5),as the Secretary of State may by order made by statutory instrument prescribe.
- (8) The Secretary of State may by regulations made by statutory instrument make provision as to the form and manner in which the Register of Floating Charges is to be maintained.
- (9) An instrument containing—
  - (a) an order under subsection (7), or
  - (b) regulations under subsection (8),is subject to annulment in pursuance of a resolution of either House of Parliament.

#### NOTE

This clause implements Recommendations 2 and 3. It provides for the setting up of the new Register of Floating Charges under the management of the Keeper of the Registers of Scotland. The form and manner in which the Register is to be organised and maintained will be the subject of regulations made by statutory instrument. The date of receipt is to be the date of registration of the relevant document (or advance notice). The intention is that (as with the Sasine Registers) the Register should record the text of the document and not (as with the Books of Council and Session) retain the document in its physical form. Subject to the stipulation of appropriate procedures, it is intended that registration can in due course be effected electronically.

## 10 Subscription of documents

In section 6 (registration of documents) of the Requirements of Writing (Scotland) Act 1995 (c.7), after paragraph (a) of subsection (1) there is inserted—

“(aa) to register a document in the Register of Floating Charges;”.

### NOTE

The Requirements of Writing (Scotland) Act 1995 provides for a form of subscription of documents whereby the document has an evidential presumption of having been validly subscribed by the signatory. Essentially, the requirement is that the signature has been witnessed. The 1995 Act provides that only documents having such "presumed authenticity" may be registered in *inter alia* the Sasine Register. In practice the same requirement is asked of documents presented to the Land Register. This clause applies the equivalent rule in the case of the Register of Floating Charges, which will facilitate a uniform treatment of applications to the Registers of Scotland when electronic conveyancing is introduced.

## 11 Floating charges over registered designs etc.

- (1) In section 19 (registration of assignments, etc.) of the Registered Designs Act 1949 (c.88), after subsection (5) there is added—

“(6) This section shall not apply in relation to any interest in a registered design arising by virtue of a floating charge granted by a document registered under section [*Register of Floating Charges*] which has not attached to the property to which it relates.”.

- (2) In section 33 (effect of registration, etc., on rights in patents) of the Patents Act 1977 (c.37), after subsection (3) there is inserted—

“(3A) Subsection (3)(b) and (c) does not include the granting of a floating charge by a document registrable under section [*Register of Floating Charges*].”.

- (3) In section 25 (registration of transactions affecting registered trade mark) of the Trade Marks Act 1994 (c.26), after subsection (2) there is inserted—

“(2A) Subsection (2)(c) does not include the granting of a floating charge by a document registrable under section [*Register of Floating Charges*].”.

### NOTE

The purpose of this clause is to implement Recommendation 12. It removes the current additional registration requirement that, in so far as it covers patents, trade marks or registered designs, a floating charge must also be registered in the appropriate register at the Patent Office. See paragraph 2.33 of the report. However, since it is conceivable that once a floating charge has crystallised the holder may wish to register the attached floating charge to establish title to the relevant intellectual property right, the wording of the amendments is designed to preserve that possibility.

## 12 Floating charges granted by industrial and provident societies

- (1) For section 3 (application to registered societies of provisions relating to floating charges) of the Industrial and Provident Societies Act 1967 (c.48) there is substituted—

**“3 Application to registered societies of provisions relating to floating charges**

- (1) The provisions of Part [*Floating charges*] (in this section referred to as the “relevant provisions”) shall apply to a registered society as they apply to an incorporated company.
- (2) Where, in the case of a registered society—
  - (a) there are in existence—
    - (i) a floating charge created under the relevant provisions (as applied by this section); and
    - (ii) an agricultural charge created under Part II of the Agricultural Credits (Scotland) Act 1929; and
  - (b) any assets of the society are subject to both charges, sections [*Ranking of floating charges(1)*] and [*Effect of floating charges on winding up(2)(c)*] shall have effect for the purposes of determining the ranking with one another of those charges as if the agricultural charge were a floating charge created under the relevant provisions on the date of creation of the agricultural charge.”.
- (2) Section 4 (filing of information relating to charges) of that Act is repealed.
- (3) In section 5 (supplemental provisions) of that Act—
  - (a) for paragraph (b) of subsection (1) there is substituted—
 

“(b) any security, except a floating charge, granted by a registered society over any of its assets,”; and
  - (b) the references to section 4 of that Act are to be treated as references to that section as it had effect immediately before its repeal by subsection (2).

**NOTE**

This clause implements part of Recommendation 11. Its purpose is to apply the recommended registration regime for floating charges by companies to floating charges in Scottish form granted by industrial and provident societies registered in Great Britain. Such charges are currently registered with the Financial Services Authority by virtue of section 4 of the Industrial and Provident Societies Act 1967, which is repealed. We also recommend that the regime should apply to floating charges granted by a limited liability partnership and a European economic interest grouping. As the relevant provisions relating to these latter bodies are contained in statutory instrument, it is anticipated that the amendments necessary to apply the new regime to them would be effected by subordinate legislation. See paragraph 2.27 of the report.

**13 Interpretation of Part 1**

In this Part—

“company” means an incorporated company (whether or not a company within the meaning of the Companies Act 1985),

“fixed security”, in relation to any property of a company, means any security (other than a floating charge or a charge having the character of a floating charge) which on the winding up of the company in Scotland would be treated as an effective security over that property including, in particular, a heritable security (within the meaning of section 9(8) of the Conveyancing and Feudal Reform (Scotland) Act 1970).

#### NOTE

This clause defines company in a way which includes an overseas company. It also defines “fixed security” in terms based on and to the same effect as the definition in section 486 of the 1985 Act.

## PART 2

### INFORMATION ABOUT SECURITIES

#### **14 Annual return to contain information about securities**

- (1) The annual return of every company registered in Scotland must contain the relevant particulars of the securities specified in subsection (2).
- (2) The securities are—
  - (a) any fixed security affecting any property of the company (but excluding a fixed security arising by operation of law), and
  - (b) any floating charge over any property of the company,  
as at the date to which the return is made up.
- (3) For the purposes of subsection (1), the relevant particulars are—
  - (a) the type of the security and the obligation it secures,
  - (b) a short description of the property to which the security relates,
  - (c) the name and address of the person in whose favour the security was granted and, if different (and if known by the company), the name and address of the present holder of the security, and
  - (d) the date on which the security was granted.

#### NOTE

This clause and the following two clauses are designed to foster financial transparency. See generally Part 4 of the report.

Subsections (1) and (2) implement Recommendation 15 of the report. Subsection (1) requires the company to supply annually a list of the securities which it has granted and which have not been discharged. This ‘securities return’ forms part of the company’s annual return made pursuant to section 363 of the Companies Act 1985 and will mean that information on securities granted by companies at the return date will be available at Companies House. A company will no longer be under a statutory duty (section 422(1) of the 1985 Act) to keep an internal register. See Recommendation 17 and clause 15.

Subsection (2) prescribes the types of securities which must be listed in the securities return, namely fixed securities and floating charges but not fixed securities arising by operation of law (such as lien or a landlord’s hypothec).

Subsection (3) implements Recommendation 16 of the report and sets out the particulars which must be included in the securities return. Details of the type of security and the date upon which the security deed was granted are required in addition to the information which should currently be found in the company’s internal register (section 422(2) of the 1985 Act). In paragraph (a), the phrase “the obligation it secures” has been employed as a security could be granted in respect of a non-pecuniary obligation. In paragraph (c), the duty to provide the name and address of the grantee and the current holder is qualified by recognition that the company which granted the security may not be aware of the identity of the current holder.

See paragraphs 4.7 – 4.10 of the report.

#### **15 Company to provide information about securities**

- (1) Every company registered in Scotland must—
  - (a) on request, and

- (b) on payment of any fee charged under subsection (3),  
supply the relevant particulars of the securities specified in subsection (2) to the person who made the request.
- (2) The securities are—
- (a) any fixed security affecting any property of the company (but excluding a fixed security arising by operation of law), and
- (b) any floating charge over any property of the company,  
granted since the date to which the most recent annual return of the company was made up (or, if the company has not made its first annual return, since incorporation of the company).
- (3) A company may charge such fees (if any) for supplying particulars under subsection (1) as it may determine subject to such limits as the Secretary of State may by order made by statutory instrument prescribe.
- (4) If a request for relevant particulars is not met—
- (a) within 10 days of the payment of any fee charged under subsection (3), or
- (b) where no such fee is charged, within 10 days of the request,  
the Court of Session may order the immediate supply of the relevant particulars to the person who made the request.
- (5) For the purposes of subsection (1), the relevant particulars are—
- (a) the type of the security and the obligation it secures,
- (b) a short description of the property to which the security relates,
- (c) the name and address of the person in whose favour the security was granted and, if different (and if known by the company), the name and address of the present holder of the security, and
- (d) the date on which the security was granted.
- (6) An instrument containing an order under subsection (3) is subject to annulment in pursuance of a resolution of either House of Parliament.

#### NOTE

Clause 15 implements Recommendation 17 of the report. Subsection (1) requires the company to supply details of any security granted since the last return date if requested to do so by any person. Thus an up-to-date picture of the company's securities can be obtained from a combination of the securities return (see clause 14) and the requested information. This supplants the need for maintenance of an internal register of charges as currently required under section 422 of the 1985 Act. Subsection (2) sets out the types of securities of which particulars can be requested. These are the same types of securities as must be listed in the annual return under clause 14(2). Subsection (3) provides that a fee may be charged for the supply of this information subject to any limit set by the Secretary of State. Subsection (4)(a) allows the company 10 days from payment of the chargeable fee to meet a request for particulars under subsection (1). Under subsection 4(b), if no fee is charged, the company must supply the details within 10 days of the request. If the company does not comply, the person who requested the information may apply to the Court of Session for an order compelling performance. Subsection (5) sets out the particulars of the security which can be requested under subsection (1). These are the same particulars as are required to be listed in the securities return under clause 14(3). See paragraph 4.11 of the report.

## **16 Company to keep copies of documents relating to securities**

- (1) Every company registered in Scotland must keep at its registered office a copy of every document granting, varying or assigning the securities specified in subsection (2).
- (2) The securities are—
  - (a) any fixed security affecting any property of the company (but excluding a fixed security arising by operation of law), and
  - (b) any floating charge over any property of the company.
- (3) The copies of documents kept under subsection (1) are to be open to inspection (on payment of any fee charged under subsection (5)) during normal business hours.
- (4) An inspection under subsection (3) is subject to such reasonable restrictions as the company may impose.
- (5) The company may charge such fees (if any) for an inspection under subsection (3) as it may determine subject to such limits as the Secretary of State may by order made by statutory instrument prescribe.
- (6) If an inspection under subsection (3) is refused, the Court of Session may order the immediate inspection of the copy of the document to which the refusal relates.
- (7) An instrument containing an order under subsection (5) is subject to annulment in pursuance of a resolution of either House of Parliament.

### **NOTE**

Clause 16 implements Recommendation 18 of the report. Part of this provision replaces section 421 of the 1985 Act which requires companies to keep copies of every security registrable under the Act. In terms of subsections (1) and (2), a company must keep at its registered office a copy of all security deeds granted by it and all deeds altering or assigning the security. The requirement applies only as respects extant securities.

Subsections (3) to (7) implement Recommendation 18(b) of the report and provide for the inspection of copies of documents kept by the company in terms of the preceding subsections. Unlike the existing statutory provision (section 423 (1) of the 1985 Act) the right of inspection is available to all.

Under subsection (3) a company must allow inspection of the copies, on payment of any fee, during normal business hours.

Subsection (4) allows a company to impose reasonable restrictions on an inspection (for example by giving the applicant a time appointment).

Subsection (5) allows the company to charge fees for an inspection. The amount of the fees may be limited by order of the Secretary of State.

In terms of subsection (6), if an inspection is refused, or so unreasonably restricted as to be equivalent to a refusal, the applicant may compel inspection through the court.

See paragraphs 4.12-4.13 of the report.

## **17 Interpretation of Part 2**

In this Part, “fixed security”, in relation to any property of a company, means any security (other than a floating charge or a charge having the character of a floating charge) including, in particular, a heritable security (within the meaning of section 9(8) of the Conveyancing and Feudal Reform (Scotland) Act 1970).

#### NOTE

This provision defines 'fixed security' for the purpose of Part 2. The definition is based on that contained in Part 1 but differs from it in respect that Part 2 is concerned with information about the grant of securities, rather than their effectiveness in a winding up, which will usually depend on whether the grantee has taken the appropriate steps by way of registration or intimation to make the right of security real and this may not be known to the company.

## **Annex D List of those to whom a link to this RIA has been sent**

100 Group  
Allen & Overy  
AM Simpson & Son  
Angel Trains Ltd  
Arden, The Rt Hon Lady Justice Mary DBE  
Association for Payment Clearing Services  
Association of British Insurers  
Association of Business Recovery Professionals  
Association of Certified Chartered Accountants  
Auditing Practices Board  
Bank Leumi (UK) plc  
Bank of England (legal unit)  
Bank of Scotland  
Barclays Bank plc  
Benjamin, Dr Joanna  
Bennett & Robertson LLP  
Benson, Ian  
Bertram, Robert  
Berwin Leighton Paisner  
Bird & Bird  
Brindle, Michael QC  
British Bankers Association  
British Vehicle Rental & Leasing Association  
  
Brown, Lyndsay  
Burness  
Carsberg, Bryan  
Chancery Division Judges  
City of London Law Society (Financial Law Committee)  
City of London Law Society (Insolvency Law Committee)  
Civil Aviation Authority  
Clifford Chance  
Clydesdale Bank PLC  
CMS-McKenna  
Commercial Bar Association  
Commercial Finance Association  
Committee of Scottish Clearing Banks  
Companies House  
Confederation of British Industry  
Consumer credit Trade Association  
CREST  
Davies, Paul  
Davies, Professor Iwan  
Deloitte & Touche  
Deutsche Trustee Company Ltd  
DLA LLP  
Dundas & Wilson  
Factors & Discounters Association  
Faculty of Advocates  
Federation of Small Businesses  
Finance & Leasing Association  
Financial Markets Law Committee  
Financial Reporting Council  
Financial Services Authority  
Forum for Private Business  
  
Freshfields Bruckhaus Deringer  
Friels  
GE Capital Aviation Services  
Goode, Professor Sir Roy  
Graham McBain  
Gretton, Professor  
Grier, Nicholas  
Gullifer, Louise  
Hampson, Stuart  
Higgs, Sir Derek  
HM Land Registry  
HPI  
HSBC  
HSBC Bank  
Iain Smith & Co  
Inland Revenue  
Institute of Chartered Accountants of England and Wales  
Institute of Company Secretaries and Administrators  
Institute of Credit Management  
Institute of Directors  
Institute of Trade Mark Attorneys  
International Factors Group  
International Underwriting Association  
International Swaps and Derivatives Association Inc  
Investment Managers Association  
Kay, Mr FAG  
Law Commission  
Law Society Company Law Committee (Working Party)  
Law Society of Northern Ireland  
Law Society of Scotland  
Linklaters  
Lloyds TSB Commercial Finance Ltd  
Lloyds TSB Group  
Lloyds TSB Scotland plc  
London Investment Banking Association  
London Stock Exchange  
Lovells  
Maclay Murray & Spens  
MacLeod, Professor,  
McBryde, Professor  
McCash & Hunter  
McJarrow & Stevenson  
Mechanical-copyright Protection Society & Performing Right Society  
Myners, Sir Paul  
National Association of Pension Funds  
National Pawnbrokers Association  
Norton Rose  
Patent Office  
Perry, Colin  
Philip, Gauld & Co  
Plender, John  
Professional Oversight Board for Accountancy  
Prudential Trustee Co Ltd

Quoted Companies Alliance  
Radcliffe, Rosemary  
Registers of Scotland  
Richards Butler  
Rickford, Jonathan  
Robert Wilson & son  
Royal Bank of Scotland plc  
Scicluna, Martin  
Scottish Law Agents' Society  
Scottish Law Commission  
Slaughter & May  
Small Business Council  
Small Business Council  
Society of Legal Scholars  
Steven, Dr Andrew  
Sykes, Richard  
Takeover Panel  
The Association of Corporate Trustees  
Trades Union Congress  
Treitel, Professor Sir Guenter  
University of Aberdeen  
Winship, Peter  
Wood, Professor Philip  
Wortley, Scott  
Ziegel, Professor Jacob

## **ANNEX E    The Consultation Code of Practice Criteria**

1. Consult widely throughout the process, allowing a minimum of 12 weeks for written consultation at least once during the development of the policy.
2. Be clear about what your proposals are, who may be affected, what questions are being asked and the timescale for responses.
3. Ensure that your consultation is clear, concise and widely accessible.
4. Give feedback regarding the responses received and how the consultation process influenced the policy.
5. Monitor the department's effectiveness at consultation, including through the use of a designated consultation co-ordinator.
6. Ensure your consultation follows better regulation best practice, including carrying out a Regulatory Impact Assessment if appropriate

The complete code is available on the Cabinet Office's web site address <http://www.cabinetoffice.gov.uk/regulation/consultation/index.asp>