

**SECURED
TRANSACTIONS CODE**

**Discussion Draft
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PART 1: CHARGES

1 The nature of a charge

- 1.1 A charge is a proprietary interest in an asset which secures the performance of an obligation and which is granted by a person (known as the chargor) over its interest in that asset in favour of another person (known as the chargee).

2 The power to create a charge

- 2.1 A chargor can create a charge over its interest in an asset in favour of a chargee to secure the performance of an obligation.
- 2.2 The chargor can be any person, subject to the limitations described in part 5.
- 2.3 The chargee can be the creditor or creditors to whom the obligation secured by the charge is owed or it may be another person (such as a trustee) for the benefit of those creditors (see part 5).
- 2.4 The asset can be existing or future property of any kind (see part 3). When the charge is created, the asset is referred to as a charged asset.
- 2.5 The chargor's interest in the asset can be any existing or future proprietary interest of any kind (see part 3). When the charge is created, the interest is referred to as a charged interest.
- 2.6 The obligation can be any existing or future obligation or liability of any kind (see part 4). When the charge is created, the obligation is referred to as a secured obligation.

3 The effect of a charge

- 3.1 Once it has been created (see part 2), a charge is effective between the chargor and the chargee.
- 3.2 Once it has been created, a charge other than a registrable charge (see part 7) is effective against:
- (a) an insolvency officer of the chargor, subject to the insolvency legislation (see part 10); and
 - (b) any other person who obtains an interest in the charged asset unless that person takes free of the charge under the priority rules (see part 8).

3.3 Once it has been created and registered under part 7, a registrable charge is effective against:

- (a) an insolvency officer of the chargor, subject to the insolvency legislation; and
- (b) any other person who obtains an interest of any kind in the charged asset unless that person takes free of the charge under the priority rules.

4 The attributes of a charge

4.1 An asset may be subject to more than one charge.

4.2 It is not necessary for the chargee to obtain possession of the charged asset.

4.3 A charge can be created over an asset even if the chargor has the authority to dispose of the asset concerned free from the charge or to deal with it in any other way.

5 The duration of a charge

5.1 Once the secured obligation has been paid or satisfied in full, the charge is automatically extinguished.

5.2 The secured obligation may consist of liabilities which are not yet in existence (see part 4). Accordingly, in the case of a running account, the charge is not extinguished just because the balance on the account is zero or the account enters into credit.

5.3 If requested to do so by the chargor after the charge has been extinguished, the chargee must execute a deed of release of the charge and assist with anything which is necessary to release the charged asset from the charge. The chargee must do these things as soon as reasonably practicable. The chargor must pay the reasonable costs of doing them unless the parties agree otherwise.

6 Distinguishing a charge from an outright interest

6.1 What distinguishes a charge from an outright proprietary interest is that the chargee's proprietary interest in the asset concerned secures the performance of an obligation.

6.2 Whether or not a proprietary interest in an asset does secure the performance of an obligation depends on the legal rights, liberties, powers and immunities of the parties to the transaction, not on the economic or functional effect of the transaction.

- 6.3 The determination of those legal rights, liberties, powers and immunities depends on the terms of the transaction concerned.
- 6.4 A proprietary interest in an asset secures the performance of an obligation if the proprietary interest is granted by a person over its interest in that asset in favour of another person (the beneficiary) and, under the terms of the transaction concerned:
- (a) a person is owed an obligation;
 - (b) the proprietary interest is an independent interest, separate from the obligation;
 - (c) the beneficiary is entitled to obtain payment of the obligation from the proprietary interest; and
 - (d) the beneficiary cannot recover more from the proprietary interest than the amount of the obligation.

7 Treating other forms of security as charges

- 7.1 If:
- (a) a person transfers a proprietary interest in an asset to another person or creates a proprietary interest over an asset in favour of that other person; and
 - (b) that proprietary interest secures the performance of an obligation,
- then it is a charge, regardless of its characterisation by the parties.
- 7.2 Accordingly mortgages, security assignments, pledges and contractual liens will be treated as charges.

8 Extent of the Code

- 8.1 Part 7 of this Code applies throughout the United Kingdom. The rest of the Code applies in England and Wales.
- 8.2 This Code does not apply to:
- (a) international interests under the International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015 (SI 2015/912); or
 - (b) security which arises by operation of law; or
 - (c) security created before the Code came into force.

PART 2: CREATION

9 Creating a charge

- 9.1 A charge is created if a chargor intends to create a charge over its interest in an asset in favour of a chargee to secure the performance of an obligation.
- 9.2 A charge is created when the chargor intends it to be created.
- 9.3 The intention of the chargor is established objectively, based on the terms of the transaction concerned.

10 Identification

- 10.1 The terms of the charge must identify the charged asset and the secured obligation.
- 10.2 This requirement is satisfied if, when the charge comes to be enforced, it is possible to establish whether or not:
- (a) a particular asset falls within the scope of the assets which are charged by the terms of the charge; and
 - (b) a particular obligation falls within the scope of the obligations which are secured by the terms of the charge.

11 Formalities

- 11.1 If the charged interest consists of or includes an interest in land, the charge must be created or evidenced by a document executed by the chargor.
- 11.2 If a charge is created by a consumer, all formal requirements imposed by consumer protection laws must be complied with.
- 11.3 If a charge is to be registered in an asset registry (see part 8), it must comply with the requirements of the asset registry concerned.
- 11.4 It is not necessary for any other charge to be created or evidenced in writing.
- 11.5 It is not necessary for the chargee to execute any document creating or evidencing a charge. Section 2 of the Law of Property (Miscellaneous Provisions) Act 1989 is amended accordingly.
- 11.6 It is not necessary for any document creating or evidencing a charge to be executed as a deed. Any legislation which requires a deed is amended accordingly.

- 11.7 Any power of attorney contained in a document which creates or evidences a charge will be effective if the document concerned is executed by the chargor. It does not have to be executed as a deed, and the Powers of Attorney Act 1971 is amended accordingly.
- 11.8 A document creating or evidencing a charge can be executed electronically.

PART 3: CHARGED ASSETS

12 Charged assets and charged interests

- 12.1 The charged asset can be property of any kind. It does not have to be located in England and Wales or governed by the laws of England and Wales. It does not have to be in existence at the time the charge is created.
- 12.2 The charged interest can be any proprietary interest of any kind. It does not have to amount to ownership. It can be legal or equitable. It can be outright or by way of security. It does not have to be in existence at the time the charge is created.
- 12.3 A chargee can create a charge over the benefit of a charge (in other words, a sub-charge).
- 12.4 A chargor can create a charge in favour of a chargee over a receivable (see section 17) owing by the chargee to the chargor.
- 12.5 A company's uncalled capital is property of the company and the company's interest in it can be charged by the company.

13 Types of asset

- 13.1 In this Code, assets are, for certain purposes, divided into:
- (a) land: which includes fixtures;
 - (b) goods: which means any tangible property which is transferable by delivery; and
 - (c) intangibles: which means any property other than land or goods.

14 Future assets

- 14.1 A chargor can create a charge over any interest which it may subsequently have in an asset. Assets of this kind are described as future assets in this Code.
- 14.2 If the terms of a charge extend to future assets, the charge will automatically cover the chargor's interest in each future asset concerned once the chargor acquires it, without the necessity for any other act by the chargor or for any further registration under part 7.

- 14.3 A chargor can create a charge over all or part of its interest in its present and future assets.
- 14.4 A chargor's future assets include assets in which it acquires an interest after it has entered into insolvency proceedings other than assets recovered in insolvency claw-back proceedings (see part 10).

15 Part of an asset

- 15.1 A charge can be created over part of an asset if that part which is charged is identifiable.
- 15.2 A particular percentage or proportion of goods or intangibles is identifiable. Unless the charge instrument provides to the contrary or the parties agree to the contrary, the chargee is entitled to all of the proceeds of the asset concerned until the chargee has received an amount equal to its percentage or proportion.

16 Extent of charged assets

- 16.1 The identity and extent of the charged asset is determined by the objective intention of the chargor, based on the terms of the transaction concerned.
- 16.2 A charge over an asset extends to the proceeds of an unauthorised disposition of that asset to the extent that they are capable of being traced under the general law.
- 16.3 A charge over an asset extends to:
- (a) the benefit of any insurance contract for the benefit of the chargor relating to that asset; and
 - (b) where the asset consists of a right to receive money, any security for that right, whether that security is proprietary (i.e. a charge) or personal (for instance a guarantee); and
 - (c) where the asset consists of the benefit of an account, the benefit of any replacement account,
- except to the extent that:
- (i) the charge instrument provides to the contrary or the parties agree to the contrary; or

- (ii) the new asset concerned is an intangible asset which cannot be charged because it is prohibited by the terms on which that asset was created (see section 19).

16.4 A charge over land extends to fixtures on the land.

17 Receivables

17.1 A receivable is the right which one person (the payee) has to be paid money by another person (the payer). The right can arise under a contract or in any other way; and it can be present, future or contingent. It includes the right to payment of a debt and a claim for damages.

17.2 If a payee creates a charge over a receivable, the chargee obtains all of the payee's rights in relation to the receivable until the charge is extinguished, subject to the terms of the charge and the provisions of this Code.

17.3 It is not a requirement for the creation of a charge over a receivable that notice of the charge is given to the payer. But notice may be given.

17.4 For the purpose of this section, a payer only receives notice of a charge once it is actually aware of it. No formalities are required, but constructive notice is not sufficient.

17.5 Until the payer has received notice of a charge, it will obtain a good discharge by paying the payee or as the payee has directed. Once the payer has received notice of a charge, it can only obtain a good discharge by paying the chargee or as the chargee has directed.

17.6 To the extent that, as a result of payment, the chargee receives more than is necessary to pay the secured obligation, it holds the balance on trust for the chargor or whoever else is entitled to it.

17.7 Once the payer has received notice of a charge, the chargee can bring legal or arbitration proceedings in its own name against the payer without the involvement of the chargor, except to the extent that the parties to the charge have agreed otherwise. To the extent necessary to resolve the proceedings, the tribunal concerned will join the chargor to the proceedings; and any costs of doing so are payable by the chargee (although it may recover them from the payee if the payee has agreed to pay them or is otherwise liable for them).

- 17.8 The chargee obtains no greater rights to the receivable than the payee has. For instance, if the payment of the receivable is subject to a condition or to a right of set-off under the contract, then the chargee is subject to them in the same way as the payee is. Accordingly, the payer cannot be required to pay a greater amount than the contract provides or (except for the identity of the payee) to pay on different terms than the contract provides.
- 17.9 In addition, the payer can set off against the chargee any other cross-claim which it has against the payee if:
- (a) the cross-claim arises under a contract or other transaction entered into before the payer has received notice of the charge (even if the cross-claim was future or contingent at the time notice was received); or
 - (b) the cross-claim is so closely connected with the chargee's claim against the payer that it would clearly be unfair for it not to be taken into account.
- 17.10 The rights, powers, liberties and immunities of the payer, the payee and the chargee under this section can be varied by agreement between the relevant parties.

18 Other assets

Provisions relating to specific types of asset can be addressed here if required, for instance in relation to registered land, ships, intellectual property and financial collateral.

19 Prohibitions on charging certain intangible assets

- 19.1 The benefit of an intangible asset (for instance, a contract) cannot be charged if it is prohibited by the terms on which the asset is created (for instance, the terms of the contract which creates it), unless it is permitted by other legislation (such as the Small Business, Enterprise and Employment Act 2015).
- 19.2 This is the case even if the prospective chargee is unaware of the prohibition.
- 19.3 Whether or not the creation of a charge is prohibited by the terms of a contract is a matter of interpretation of the contract concerned.
- 19.4 If the creation of a charge over all or any part of the benefit of an intangible asset is prohibited by terms on which the asset was created, then:

- (a) unless it is permitted by other legislation, any purported charge is, to the extent of the prohibition, invalid; and
- (b) if the chargor has agreed to create the charge, the invalidity of the charge may result in a personal claim by the intended chargee against the chargor.

19.5 In this Code, a prohibition on the creation of a charge includes any limitation of any kind on the creation of the charge (including, for instance, the requirement for a consent which has not been obtained).

19.6 This section does not apply to the proceeds of a receivable once they have been paid.

20 Other contractual prohibitions on charging assets

20.1 Neither the validity nor the priority of a charge over an asset is affected by any contractual prohibition on the creation of a charge by a chargor, except to the extent that it is invalidated under the preceding section.

20.2 This is the case even if the chargee is aware of the prohibition.

20.3 This does not affect any personal claim for breach of contract which the chargor may be liable for.

20.4 If:

- (a) a chargor creates a charge over an asset; and
- (b) a person with a proprietary interest in that asset has the benefit of a contractual prohibition on the creation of such a charge; and
- (c) when taking the charge, the chargee had actual knowledge of that prohibition and deliberately encouraged the chargor to breach it,

then the chargee is liable in tort for the loss suffered by the person in whose favour the prohibition was given. The chargee has no other liability of any kind (for instance, in tort or in equity) if it takes a charge in breach of a contractual prohibition on its creation.

CONTRACTUAL RESTRICTIONS ON CHARGING ASSETS: ALTERNATIVE APPROACH

(This would replace sections 19 and 20)

19. Contractual restrictions on charging assets

19.1 *A contractual restriction on the creation of a charge does not affect the validity of the charge. The charge is valid in spite of the restriction, even if the chargee is aware of the restriction.*

19.2 *If:*

(a) *the charged asset is a receivable arising under a contract (a contractual receivable); and*

(b) *the charge breaches a restriction in that contract on the creation of the charge, the payer cannot be required to pay anyone other than is provided for in the contract until the chargee enforces the charge and notifies the payer that it has done so. Once this has happened, the payer must pay the chargee (or as it directs). In addition to the set-offs available to any payer against a chargee, the payer may also set off against the chargee any monetary claim it has against the chargor at the time payment is due which it could have set off against the chargor if the receivable had not been charged. This includes insolvency set-off if the chargor, the chargee or the payer has entered into insolvency proceedings.*

19.3 *If:*

(a) *the charged asset is an intangible arising under a contract with a third party but is not a contractual receivable; and*

(b) *the charge breaches a restriction in that contract on the creation of the charge, the third party cannot be required to do anything which would put it in a worse position than the contract provides.*

19.4 *If the chargor commits a breach of a contractual restriction on the creation of a charge by entering into the charge, the chargor is liable to the person in whose favour the restriction was given for the loss suffered by that person as a result.*

19.5 If:

- (a) a chargor creates a charge over an asset; and
- (b) a person with a proprietary interest in that asset has the benefit of a contractual restriction on the creation of such a charge; and
- (c) when taking the charge, the chargee had actual knowledge of that restriction and deliberately encouraged the chargor to breach it,

then the chargee is liable in tort for the loss suffered by the person in whose favour the restriction was given. The chargee has no other liability of any kind (for instance, in tort or equity) to any person if it takes a charge in breach of a contractual restriction on its creation.”

PART 4: SECURED OBLIGATIONS

21 Secured obligations

- 21.1 The secured obligation can be any obligation or liability of any kind of any person. It can be an existing liability (whether present, future or contingent) or it may be a liability which is not yet in existence (and which may, or may not, come into existence in the future).
- 21.2 For example, a secured obligation may include a liability to pay all money from time to time owing:
- (a) to a particular person or class of persons; or
 - (b) under a particular agreement or class of agreements.
- 21.3 The secured obligation does not have to be owed by the chargor. Nor does it have to be owed to the chargee.
- 21.4 The identity and extent of the secured obligation is determined by the objective intention of the chargor, based on the terms of the transaction concerned.
- 21.5 If the secured obligation is not an obligation to pay money, the charge secures the obligation to pay damages for breach.

PART 5: PARTIES

22 The chargor

- 22.1 A charge can be created by any person, subject to the limitations contained in this part and to any limitations contained in other legislation.
- 22.2 An individual cannot create a charge over an interest in goods in England and Wales unless:
- (a) the goods are owned by the chargor at the time the charge is created; or
 - (b) the chargor is carrying on business as a sole trader and the goods concerned are assets of the business concerned; or
 - (c) the chargor is a member of a partnership or a limited partnership and the goods concerned are assets of the partnership concerned.

23 The chargee

- 23.1 A charge can be created in favour of:
- (a) the creditor or creditors to whom the obligation secured by the charge is owed (the creditors); or
 - (b) another person (such as a trustee) for the benefit of the creditors.
- 23.2 A person can hold the benefit of a charge on behalf of any number of present, future or contingent creditors.
- 23.3 The rights, powers, liberties and immunities of that person and the creditors between themselves can be established and varied by agreement between them.

PART 6: TERMS

24 The terms

- 24.1 Subject to the provisions of this Code and of any other relevant laws and regulations (such as those concerning consumers), the terms of the charge can be agreed between the parties from time to time.
- 24.2 In the absence of agreement, the chargor may not do anything which materially prejudices the existence and priority of the charge, but may otherwise deal with the charged asset in any way until the charge is enforced.
- 24.3 In the absence of agreement, the chargee has no power to deal with the charged asset until the charge is enforced.
- 24.4 The doctrine of clogs on the equity of redemption is abolished.

PART 7: REGISTRATION

25 Registration of certain businesses

- 25.1 In this Code, the registrar is the Registrar of Companies.
- 25.2 The following types of business may register at Companies House for the purposes of the Code:
- (a) a company or corporation incorporated by statute or created by Royal charter in any part of the United Kingdom;
 - (b) a partnership or limited partnership which is created under the law of any part of the United Kingdom;
 - (c) an individual who is carrying on business as a sole trader wholly or partly in the United Kingdom.
- 25.3 Businesses of this type are described in the Code as registrable businesses.
- 25.4 The process of the registration of a registrable business will be determined by the registrar, and may be amended from time to time.
- 25.5 Once the process of registration of a registrable business has been completed, the registrar will issue that registrable business with a registered number.
- 25.6 A registrable business which has been registered at Companies House is described in the Code as a registered business.
- 25.7 The only purpose of registration under this section is to enable the registration of charges by registered businesses. It has no other significance.

26 UK Businesses

- 26.1 A UK business is:
- (a) a UK-registered company within the meaning of section 1158 of the Companies Act 2006;
 - (b) a limited liability partnership registered in any part of the United Kingdom;
 - (c) a registered business.

27 Registrable charges

- 27.1 Every charge created by a UK business is a registrable charge unless it is an exempt charge.
- 27.2 A charge is an exempt charge if it is:
- (a) a possessory charge; or
 - (b) a financial collateral charge; or
 - (c) a rent deposit charge; or
 - (d) a Lloyd's charge; or
 - (e) a central bank charge; or
 - (f) a charge which is exempt from registration under this Code as a result of other legislation.

[It may be helpful to add another exception to cover electronic bills of lading]

- 27.3 A charge created by a registrable business is only a registrable charge if it is created after that registrable business has become a registered business.
- 27.4 A charge is not created by a UK business if:
- (a) the charge arises by operation of law; or
 - (b) the UK business acquires an asset which is already subject to the charge; or
 - (c) the UK business is the owner of property and, in connection with a dealing with that property, it retains an interest in the property to secure the payment of a secured obligation.

28 Possessory charge

- 28.1 A charge is a possessory charge to the extent that the chargee has possession of the charged asset at the time the issue is to be determined.
- 28.2 A person has possession of charged assets if:
- (a) they are goods, and it has physical possession of them; or

- (b) they are goods, and it has possession of them by attornment; or
- (c) they are goods or intangibles, and it has documentary possession of them.

28.3 A person (A) has possession of goods by attornment if:

- (a) someone other than the chargor or the chargee (B) has physical possession of them; and
- (b) with the consent of the chargor, B has acknowledged to A that B holds them on behalf of A.

The acknowledgement can be in writing, but does not have to be.

28.4 A person has documentary possession of goods or intangibles if:

- (a) it has physical possession of a document of title to them (for instance, a bill of lading, a bearer security or a negotiable instrument); and
- (b) that document is either made out to bearer or made in favour of the person concerned (whether initially or by endorsement).

28.5 A person who has possession of a charged asset does not cease to have a possessory charge only because:

- (a) the asset is taken from it without its consent; or
- (b) the asset is sub-charged by that person to someone other than the chargor with the consent of the chargor; or
- (c) the asset is delivered to the chargor for the purpose of sale and on the basis that the net proceeds of sale are held on trust for the chargee.

29 Financial collateral charge

29.1 A charge is a financial collateral charge if it is created or arises under a security financial collateral arrangement.

29.2 Security financial collateral arrangement has the meaning given to it in The Financial Collateral Arrangements (No 2) Regulations 2003 (SI 2003/3226) as amended from time to time.

30 Rent deposit, Lloyds and central bank charges

- 30.1 A rent deposit charge is a charge in favour of a landlord on a cash deposit given as security in connection with the lease of land.
- 30.2 A Lloyd's charge is a charge created by a member of Lloyd's (within the meaning of the Lloyd's Act 1982) to secure its obligations in connection with its underwriting business at Lloyd's.
- 30.3 A central bank charge is a charge which falls within section 252 of the Banking Act 2009, as amended from time to time.

31 The effect of non-registration

- 31.1 Until it has been registered, a registrable charge is of no effect against any person other than the parties.
- 31.2 In particular, until it has been registered, a registrable charge is of no effect against:
- (a) an insolvency officer of the chargor (see part 10); or
 - (b) any other person who obtains an interest of any kind in the charged asset.
- 31.3 This is the case even if the person concerned was aware of the existence of the charge.

32 Registration procedure

- 32.1 Where a UK business has created a charge, the chargee, the chargor or a person acting on behalf of either of them (a registrant) may deliver to the registrar:
- (a) a certified copy of the instrument creating the charge (or, if there is no instrument, evidence of the creation of the charge); and
 - (b) a document specifying:
 - (i) the registered name and number of the chargor;
 - (ii) the name of the chargee;
 - (iii) the date of creation of the charge; and

- (iv) whether the charge is expressed to cover all, or substantially all, of the present and future assets of the chargor.

32.2 This can be done even if the charge concerned is an exempt charge.

32.3 The certified copy of the charge instrument can be redacted to omit:

- (a) personal information relating to an individual (other than the name of the individual);
- (b) the number or other identifier of a bank or securities account;
- (c) a signature.

32.4 On receipt of those documents, the registrar will register them and will deliver to the registrant an electronic confirmation that the registrar has received those documents and the time of receipt.

[It is intended that the chargee will receive confirmation of registration automatically as soon as the documents are delivered.]

32.5 The charge becomes registered on receipt by the registrant of that electronic confirmation.

32.6 That confirmation is conclusive evidence that the charge has been duly registered and of the time of registration.

33 Priority notices

33.1 The registrant may deliver to the registrar a notice of an intention to create a charge in advance of the charge being created. That notice is described as a priority notice in this Code. The priority notice must state the registered name and number of the chargor and the name of the chargee.

33.2 On receipt of a priority notice, the registrar will register it and will deliver to the registrant an electronic confirmation of the time of registration of the priority notice.

33.3 If a charge is created by that chargor in favour of that chargee and is registered within 30 days after the registration of the priority notice, the charge will be deemed to have been registered at the time that the priority notice was registered for the purpose of the priority rules contained in part 8.

34 Amendments and priority agreements

34.1 If:

- (a) an amendment is made to the terms of a registrable charge; and
- (b) the amendment extends the scope of the charged asset or the secured obligation,

then the amendment must be registered in accordance with this part 7 because, to the extent that it does so, it creates a new charge.

34.2 If any other amendment is made to the terms of a registrable charge, the registrant may deliver a certified copy of the amendment to the registrar, who will register it. Whether or not this is done does not affect the validity of the charge or the conclusive nature of the existing certificate of registration.

34.3 If a priority agreement is entered into in relation to one or more registrable charges (see part 8), the registrant may deliver to the registrar either a certified copy of the agreement or a notice that a priority agreement has been entered into, in which event the registrar will register it with each registrable charge to which it relates. Whether or not this is done does not affect the validity or effectiveness of the priority agreement.

35 Releases of charges

35.1 The registrant may send to the registrar a notice that:

- (a) the charge has been released; or
- (b) specified assets have been released from the charge.

35.2 If the registrar has received confirmation from the chargee (or from a person acting on behalf of the chargee) that the notice is correct, the registrar will, as soon as reasonably practicable, register it and confirm that he has done so to the registrant.

[It is sometimes impossible to get the confirmation of a chargee even where the charge has clearly been extinguished. It should be possible to tidy-up the register without confirmation from the chargee if there are appropriate safeguards.]

PART 8: PRIORITIES

36 The scope of this part

36.1 This part deals with the following priority issues:

- (a) priorities between charges;
- (b) priorities between a charge and a subsequent outright disposition of assets subject to the charge.

36.2 These priority issues are determined in accordance with this Code, which overrides any priority rule which would otherwise have applied under the general law.

36.3 If a registrable charge has not been registered in accordance with part 7, it is of no effect against third parties. Accordingly, references to charges in this part are to:

- (a) registrable charges which have been registered under part 7; and
- (b) charges other than registrable charges.

37 Agreement

37.1 The provisions contained in this part can be varied by agreement between the parties concerned. That agreement can be made and varied at any time.

37.2 If the charged interest or the charged asset is registrable in an asset registry, this is subject to the rules of the relevant asset registry.

38 Priorities between charges

38.1 If more than one charge has been created over the same charged asset, the priority of the charges between themselves is determined by the following Rules.

38.2 Rule 1: If a charged asset is registrable in an asset registry, priority between charges over the asset concerned is determined by the rules of the relevant asset registry, to the extent that those rules resolve the priority issue concerned.

38.3 Rule 2: [If a charged asset is financial collateral and a chargee obtains control over the asset concerned, that chargee will take priority over any other chargees of that asset.]

- 38.4 Rule 3: In any other case, the priority of charges between themselves depends on the times they are created or (in the case of a registrable charge) registered under part 7. The first to be created or (in the case of a registrable charge) registered takes priority.
- 38.5 When applying these rules to a charge, it makes no difference that the chargee has authorised the chargor to dispose of charged assets free of the charge.
- 38.6 The asset registries are:
- (a) Her Majesty's Land Registry;
 - (b) the register of British ships;
 - (c) the register of aircraft mortgages maintained by the Civil Aviation Authority;
 - (d) the registers of patents and of trade marks maintained by the Comptroller-General of Patents, Designs and Trade Marks.

39 Tacking further advances

- 39.1 If a charge has priority over another proprietary interest (whether outright or by way of security), that priority extends to the entire secured obligation secured by the charge, regardless of the time advances were made.
- 39.2 All restrictions on tacking further advances are abolished.

40 Transactions for which no value is given

- 40.1 If a person purports to acquire a proprietary interest in a charged asset from a chargor for no consideration (for instance as a gift), that person takes its proprietary interest subject to the charge.
- 40.2 If a person obtains execution of any kind over a charged asset, the execution is subject to the charge.
- 40.3 This section is subject to regulation 35 of the Uncertificated Securities Regulations 2001 (2001/3755) and the rules or specifications contemplated by paragraphs 5(3) to (5) of Schedule 1 to those Regulations.

41 Outright dispositions of assets

- 41.1 If a person (the acquirer) purports to acquire an outright proprietary interest in a charged asset from a chargor which is not in insolvency proceedings (see part 10), the acquirer will only obtain its interest in the asset free from the charge if:
- (a) the chargor had the actual or apparent authority from the chargee to effect the transaction; or
 - (b) in the case of a fixed asset, the following section applies; or
 - (c) in the case of a current asset, the next section but one applies.
- 41.2 A charged asset is a current asset if it is:
- (a) [financial collateral]; or
 - (b) goods other than ships or aircraft objects which, in the transaction concerned, a reasonable acquirer would expect the chargor to be able to sell free from a charge without the acquirer having to check whether the chargor has the actual or apparent authority from the chargee to effect the transaction.
- 41.3 A charged asset is a fixed asset if it is not a current asset.
- 41.4 An outright proprietary interest is any proprietary interest other than a charge.

42 Outright dispositions of fixed assets

- 42.1 If a person (the acquirer) purports to acquire an outright proprietary interest in a fixed asset from a chargor which is not in insolvency proceedings, the acquirer will obtain its interest free from the charge unless, at the time of the purported acquisition:
- (a) the charge was on the register at Companies House or at an asset registry; or
 - (b) the acquirer actually knew the asset was subject to a charge; or
 - (c) the acquirer had constructive notice that the asset was subject to a charge.
- 42.2 A person will only have constructive notice that an asset is subject to a charge if that person would have discovered the existence of the charge if it had made all those enquiries which it ought reasonably to have made before entering into the transaction concerned. What is reasonable depends on all the circumstances relating to the

transaction (for instance, the identity of the parties, the nature of the assets concerned and the size of the transaction).

43 Outright dispositions of current assets

43.1 If a person (the acquirer) purports to acquire an outright proprietary interest in a current asset from a chargor which is not in insolvency proceedings, the acquirer will obtain its interest free from the charge unless:

- (a) the acquisition is prohibited in a contract entered into between the chargor and the chargee (a restriction on disposal); and
- (b) the acquirer actually knew of the restriction on disposal at the time of the purported acquisition.

43.2 Nothing in this section absolves the chargor from the consequences of any breach of contract which it commits as a result of breaching a restriction on disposal.

43.3 In the absence of fraud (in the sense of dishonesty), the acquirer is not liable to any person for any breach of a restriction on disposal of a current asset by the chargor (whether in tort, in equity or in any other manner).

44 Other priority issues

44.1 Any priority issues which are not determined by the Code will be determined under the general law.

44.2 For this purpose, to the extent that it is relevant, a charge will be treated as a legal interest.

[We could try to codify the law further if there is a consensus as to how to do it.]

PART 9: ENFORCEMENT

45 The scope of this part

- 45.1 This part applies to the enforcement of charges, except to the extent that other laws (for example those concerning financial collateral, financial markets or settlement finality) provide to the contrary.
- 45.2 Where the chargor is an individual, this part is subject to all laws concerning consumers.

46 Time for enforcement

- 46.1 A chargee can enforce a charge at the time provided for it in the charge instrument, or as otherwise agreed by the chargor.
- 46.2 If there is no such provision or agreement, the chargee can enforce the charge as soon as:
- (a) all or any part of the secured obligation is to be performed; and
 - (b) the person liable to perform the secured obligation has received notice requiring it to be performed; and
 - (c) unless the chargor is insolvent or admits it is unable to perform the secured obligation in full, two business days have elapsed from the receipt of that notice, and the secured obligation has not been performed in full.

47 Enforcement powers

- 47.1 A chargee can enforce a charge in the manner provided for in the charge instrument, or as otherwise agreed by the chargor.
- 47.2 If there is no such provision or agreement, a chargee has the following powers:
- (a) to the extent permitted by the insolvency legislation (see part 10), to appoint an administrator or administrative receiver of the chargor; and
 - (b) to appoint a receiver over all or any part of the charged interest in the charged assets; and
 - (c) to apply to court for the sale of the charged assets; and

- (d) to take all such other actions (or to refrain from doing so) in relation to all or any part of the charged assets as the chargor could have done if they were not charged (for instance by taking possession of them, selling them or leasing them; exercising a power of netting; in the case of receivables, demanding and receiving payment; and, in the case of cross-claims, setting them off).

47.3 These powers do not apply to the extent that they are inconsistent with the terms of the charge or the agreement of the parties. They can be increased, reduced, disapplied or amended in any other way in the terms of the charge or by agreement between the parties.

47.4 For the purpose of enforcing a charge, the chargee can:

- (a) transfer or procure the transfer of the legal title to a charged asset if the entire beneficial interest in the asset concerned has been charged; and
- (b) execute a deed even if the charge was not created by a deed.

47.5 To the extent that the charge is a financial collateral charge (see part 7), the chargee also has the powers (for instance, the power of appropriation) conferred on it by the Financial Collateral Arrangements (No 2) Regulations 2003 (SI 2003/3226) as amended from time to time.

47.6 The power to take possession of a dwelling-house is subject to the restrictions contained in section 36 of the Administration of Justice Act 1970, as amended by section 8 of the Administration of Justice Act 1973.

47.7 Foreclosure is abolished.

48 Powers of administrators and receivers

48.1 Administrators have the powers conferred on them by the insolvency legislation.

48.2 Administrative receivers and receivers each have the powers conferred on them by the terms of the charge or by agreement with the chargor.

48.3 Except to the extent that they are amended by the terms of the charge or by agreement with the chargor:

- (a) administrative receivers and receivers each have the power to take all such actions (or refrain from doing so) in relation to all or any part of the assets over

which they are appointed as the chargor could have done if they were not charged (for instance by taking possession of them, selling them or leasing them; exercising a power of netting; in the case of receivables, demanding and receiving payment; and, in the case of cross-claims, setting them off); and

- (b) (without limitation) administrative receivers have the powers conferred on them by the insolvency legislation (see part 10).

48.4 An administrator, an administrative receiver and a receiver can:

- (a) transfer legal title to a charged asset if the entire beneficial interest in the asset concerned has been charged; and
- (b) execute a deed even if the charge was not created by a deed.

48.5 The power to take possession of a dwelling house is subject to the restrictions contained in section 36 of the Administration of Justice Act 1970, as amended by section 8 of the Administration of Justice Act 1973.

49 More than one charge

49.1 Where there is more than one charge over the same charged asset, the charged asset can be sold free from any charges which rank behind the charge concerned. If this happens, the rights of the subsequent chargees are transferred from the charged asset to its proceeds of sale.

49.2 Where there is more than one charge over the same charged asset, the charged asset can be sold under a second or subsequent charge subject to any charges which rank in priority.

49.3 This section is subject to any agreement to the contrary between the relevant parties.

50 Effect on third parties

50.1 An administrative receiver of a chargor and a receiver of charged assets is the agent of the chargor (even if the chargor enters into insolvency proceedings).

50.2 A person dealing with a chargee, or with a receiver or administrative receiver, is entitled to assume, unless it has actual knowledge to the contrary, that:

- (a) those persons have the power to do those things which they are purporting to do;
and
- (b) they are exercising their powers properly.

51 Duties on enforcement

- 51.1 When enforcing a charge over charged assets, the person doing so (the enforcer) owes a duty to each interested person to take reasonable care of the charged assets which are the subject of the enforcement.
- 51.2 An interested person is:
- (a) the chargor (where it is in insolvency proceedings, acting through its insolvency officer – see part 10); and
 - (b) any chargee of the charged assets other than the enforcer; and
 - (c) any person (such as a guarantor) who is liable for all or part of the secured obligations concerned.
- 51.3 When selling charged assets, the enforcer owes a duty to each interested person to obtain the best price reasonably obtainable for the charged assets at the time of sale.
- 51.4 The enforcer can sell the charged assets when it decides to do so. It has no duty to accelerate or delay a sale even if to do so might increase the sale proceeds.
- 51.5 Any claim for breach of these duties by the enforcer must be brought by or on behalf of an interested person for the amount of loss suffered by that person as a result of the breach of duty. For this purpose, loss suffered by an insolvent chargor includes loss suffered by its creditors (except to the extent that they are themselves interested persons and bring their own claim).
- 51.6 An enforcer can sell charged assets to a person connected with the chargee or with anyone else with an interest in the charge. If it does so, it must have contemporaneous evidence from an independent person qualified to give it that, in that person's opinion, it has obtained the best price reasonably obtainable for the charged assets at the time of sale.
- 51.7 Where the charged assets consist of financial collateral, this section is subject to the rules concerning enforcement contained in the legislation concerning financial

collateral. It is also subject to Part VII of the Companies Act 1989 and to the Financial Markets and Insolvency (Settlement Finality) Regulations 1999.

51.8 This section is subject to any agreement to the contrary between the relevant parties.

[Add a power for the chargee to “appropriate” the charged assets, subject to proper safeguards for the chargor.]

PART 10: INSOLVENCY PROCEEDINGS

52 Effectiveness of charges

52.1 A charge creates a proprietary interest in the charged asset and it remains effective until it is extinguished, even if the chargor is in insolvency proceedings.

52.2 If the chargor does enter into insolvency proceedings, the rights of the chargee in relation to the charge are subject to the insolvency legislation.

52.3 In this Code:

(a) insolvency legislation means:

- (i) the Insolvency Act 1986 and secondary legislation made under it;
- (ii) the European Insolvency Regulation (Regulation (EU) 2015/848 of 20 May 2015) as it may be amended from time to time; and
- (iii) any other primary or secondary legislation in force in England from time to time relating to, or affecting, insolvency or reorganisation.

(b) insolvency proceedings means:

- (i) where the chargor is a natural person, bankruptcy; and
- (ii) in any other case, liquidation or administration;

(c) insolvency officer means a trustee in bankruptcy, liquidator or administrator of a chargor;

(d) insolvency claw-back proceedings means the proceedings described in section 53.

53 Insolvency claw-back proceedings

53.1 Under the insolvency legislation, a charge may be set aside in whole or in part (and other remedies may be available) if:

- (a) the charge is a voidable preference (see Insolvency Act 1986, sections 239 and 340); or

- (b) *[the charge secures old money – perhaps limited to a charge over all or substantially all of the chargor’s assets]; or*
- (c) the charge is a transaction at an undervalue (see Insolvency Act 1986, sections 238 and 339); or
- (d) the charge is part of a transaction defrauding creditors (see Insolvency Act 1986, section 423).

[Time limits for claw-back will need to start on the date of registration for registrable charges.]

54 Limitations of enforcement

- 54.1 If the chargor is a company which goes into administration, there are limitations on the chargee’s power to enforce the charge (see Insolvency Act 1986, paras 43 and 44 of Schedule B1).
- 54.2 There are similar limitations where a small company proposes to enter into a voluntary arrangement (see Insolvency Act 1986, Schedule A1).
- 54.3 *[Bank resolution proceedings]*

55 Use of charged assets by a liquidator or administrator

- 55.1 *It is envisaged that section 55 will contain a power for an administration (and possibly a liquidator) to use a certain amount of charged assets in certain limited circumstances. As an interim measure, we may need to draft a provision which broadly replicates the way in which floating charge assets are dealt with on an insolvency.*

Note: Cross-border transactions

Cross-border transactions are so important in practice that it is considered desirable to add a further part to the Code – Part 11: Cross-Border Transactions – to deal with the conflict of laws. There are difficult issues here – not least its relationship with EU law – and it has been decided not to propose drafting at this stage but first to see if it is possible to reach a consensus on what is both feasible and desirable.