# Goods Mortgages Bill

## July 2017

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## Introduction

This is the Bill to repeal the Bills of Sale Acts 1878 and 1882 (which provide for the creation of security by individuals over goods or chattels which remain in their possession) to modernise the old legislation by imposing fewer burdens on lenders and granting more protection for borrowers.

A draft of the Bill was published on 4 July 2017. It appears to contain most of the clauses other than those dealing with registration of mortgages; these clauses are likely to be published after there is a specific consultation over having a new electronic register and/or an updated court service for searching the court register. The consultation period for the published clauses ends on 7 August 2017, as the Law Commission hopes to put the Bill before Parliament in the Autumn. Given that it is only a Bill, the published clauses are subject to change

## Overview

The Bill permits an individual who owns "qualifying goods" to create a charge over them (a "goods mortgage") as security to discharge an obligation. It is important to note that the goods have to be in existence (i.e. future goods cannot be charged) and a person only having an equitable interest under a trust cannot create a goods mortgage. If qualifying goods are owned by two or more persons they can together create a goods mortgage over the goods or one of them can charge his individual share.

The term "qualifying goods" includes tangible moveable property (such as works of art) provided they are in England and Wales when the charge is created, but excludes aircraft, ships and currency notes or coins that are legal tender.

Unlike bills of sale, the goods mortgage will be able to secure a fluctuating loan amount and a floating rate of interest.

Certain obligations cannot be secured by a goods mortgage:

- obligations under a guarantee unless the high net worth conditions in clause 28(4) are met and the goods mortgage contains a declaration by the mortgagor that certain protections and remedies are not available and that certain prescribed requirements have been complied with; and

- obligations under a running account credit unless the high net worth conditions above are met or the business credit conditions in clause 28(5) are met and the goods mortgage contains a declaration in similar form to the above.

Broadly speaking the high net worth and business credit tests are similar to those under the Financial Services and Markets Act 2000.

The goods mortgage must be in writing and comply with the requirements of clause 5 and (unless it is an exempt goods mortgage under clause 28) the regulations to be made thereunder. The requirements are more simplified than for bills of sale, although they must contain prominent warnings (as is the case with real property mortgages). Specifically, the goods mortgage document should contain:

1. the date of the goods mortgage;

2. the names and addresses of the borrower and lender;

3. a description of the obligation which is secured by the goods mortgage;

4. the name and address of the witness;

5. a specific description of the goods; and

6. the relevant prominent statements (unless the goods mortgage is an "exempt" goods mortgage – clause 5(3)).

In the case of art it will be extremely important to describe the work properly so that it can be found in a search. Some lenders may seek to tag works so that there is a unique description and record which can be easily traced.

Clause 6 of the Bill contains anti-avoidance provisions so that disguised goods mortgages not complying with the Bill will be void. An example is a sale and lease back. The goods must be in the possession of the borrower, so liens and pledges are not affected by the Bill.

The Bill contains a distinction between "general goods mortgage" and a "vehicle mortgage", but this briefing focuses on general goods mortgages only (i.e. not mortgages of vehicles).

As mentioned above, details of the registration procedure for general goods mortgages will be contained in clause 9 of the Bill, but this is subject to further consultation with third parties.

Clause 15 contains provisions protecting a private purchaser of goods which are the subject of a goods mortgage if either:

a) the goods mortgage was not registered; or

b) the purchaser purchased the goods in good faith without **actual** notice that the goods are subject to a goods mortgage in which event the purchaser takes free of the goods mortgage.

This was primarily aimed at protecting private purchasers of motor vehicles, but will apply to all goods. This clause could potentially be problematic to a lender, because registration of a goods mortgage is unlikely to constitute **actual** notice to a private purchaser.

Clause 17 provides that the goods mortgage is void against the mortgagor's trustee in bankruptcy unless it was registered when the bankruptcy application is made or the petition is presented.

Part 4 of the Bill contains provisions to protect mortgagors.

Clause 18 provides that a mortgagee is not entitled to the possession of the goods unless:

a) a payment is overdue;

b) a failure to maintain insurance as per the goods mortgage;

c) goods moved by the mortgagor in breach of terms of goods mortgage;

d) goods offered for sale without consent;

e) non-financial obligation is undischarged;

f) goods liable to be seized; or

g) mortgagor bankrupt or equivalent.

Clause 19 provides that a mortgagee is not entitled to enter premises to take possession of goods without a court order.

Clauses 20 and 21 set out the procedure required to be followed before a mortgagee can obtain possession of goods.

Briefly, a mortgagee is required to give a "possession notice" to the mortgagor before taking possession of goods unless the requirements of clause 20(2) are met. These requirements are:

a) if the following conditions are met:

i. the secured obligation can be discharged by the payment of money,

ii. the redemption total is ascertainable when goods mortgage is created; and

iii. at the time possession is taken less than one-third of redemption total has been paid, **OR**

b) the goods mortgage is an "exempt goods mortgage" (clause 28).

Under clause 28 an exempt goods mortgage is:

a) one where the obligation secured is a guarantee or a running-account credit; or

b) one where the high net worth conditions are met (under clause 28(4)); or

c) the business credit conditions are met (under clause 28 (5)); and

d) one which contains a declaration by the mortgagor that it foregoes certain protections and remedies relating to the possession notice and mortgagor's rights on termination; and

e) one which complies with prescribed requirements.

It follows that, for example, a loan to a high net worth individual secured on a work of art is likely to be an exempt goods mortgage which will result in the lender not being fettered by having to serve a possession notice or obtaining a court order to obtain possession of the art. The mortgagee would, however, still need a court order to enter premises other than with the mortgagor's consent.

If the goods mortgage is not an exempt goods mortgage OR one third or more of the redemption total has been paid, the mortgagee will need to give a possession notice to the mortgagor (in the prescribed form) before taking possession of the goods. The possession notice has to contain certain prescribed information including informing the mortgagor of his right to terminate pursuant to clause 27 and that the mortgagor may within the "prescribed period" require the mortgagee not to take possession of the goods without a court order or his right to inform the mortgagor of his intention to seek advice. The effect of these provisions is to give the mortgagor a moratorium to enable the mortgagor to seek advice and require the mortgagee to obtain a court order in order to obtain possession of the goods. The court has a wide discretion to adjourn proceedings, to suspend execution of the judgment or order or to postpone the date for delivery of possession of the goods in each case for such period as it considers reasonable. If the mortgagee breaches clauses 18 *(Restriction on mortgagee taking possession)*, 20 *(Possession notice required before taking possession)* or 21 *(Possession notice)*, the draconian effect is that the mortgagor is entitled to have the goods returned and is released from all further liability under the goods mortgage (clause 23).

Clause 22 covers the position where a goods mortgage is given to secure a payment under a regulated agreement under the Consumer Credit Act 1974 and there is a default under such regulated agreement.

Clauses 25 and 26 provide for the mortgagee's power of sale under a goods mortgage and restrictions on that power. Once the mortgagee obtains possession of the goods, it has power to sell them, provided the goods mortgage has been duly registered.

A subsequent mortgagee of the goods needs the consent of a prior mortgagee to sell the goods, unless it obtains a court order. As with the Bills of Sale Acts, a mortgagee taking possession of the goods has to wait 5 working days before selling them which gives the mortgagor the opportunity to apply to the court for relief. These clauses apply to every goods mortgage including an exempt goods mortgage.

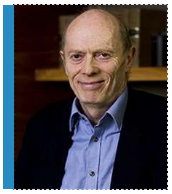
Clause 27 gives a mortgagor under a goods mortgage (other than an exempt goods mortgage) the right to terminate it in certain circumstances and deliver the goods to the mortgagee. The effect of this is that on termination, the mortgagor is released from any further liability under the obligation secured by the goods mortgage and title to the goods passes to the mortgagee.

As you would expect, clause 29 provides that contracting-out of the Act is forbidden.

## Conclusion

The Bill is a welcome reform of the archaic Bills of Sale Acts. So far as lenders against art are concerned, provided they ensure that their goods mortgage falls within the definition of “exempt goods mortgage”, they can lend to an individual borrower who wishes to keep his art on the wall with more certainty that they have an effective security interest whilst the protections granted to the mortgagor should not be too onerous from their standpoint.  One potential concern for a lender, however, is whether a fraudulent mortgagor could pass good title to a private purchaser under clause 15 and thereby defeat the lender's goods mortgage. We await to see what is proposed in relation to registration of goods mortgages.  It is worth noting that nothing in the new Bill prevents a lender from taking security by way of pledge from an individual where the lender has actual or constructive possession of the goods.

## Contacts



**Andrew Evans**
Partner - London

E: andrew.evans@fieldfisher.com
T: +44 (0)20 7861 4169
M: +44 (0)7780 997 043

**Hannah Rowbotham**
Senior Associate - London

E: hannah.rowbotham@fieldfisher.com
T: +44 (0)20 7861 4649
M: +44 (0)7725 619 636

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