

## Introduction

Guernsey law is nowadays very influenced by English law. However, in the context of security over real property, the method by which the security is taken, the nature of the security and the means of realising the security are all very different from their English equivalents. In this paper we will discuss the method by which security is taken over real property and the means by which security is realised when the need to do so arises.

## Distinction between real and personal property

In brief, real property comprises land and buildings (including houses) as opposed to personal property, which comprises everything which is not real property. The question of whether, and if so how, security can be taken over personal property in Guernsey is a complex one and is outside the scope of this paper.

## The system of taking security over real property

Security is generally taken over real property in Guernsey by means of a “bond”. There is no particular magic about the word “bond”. A bond is simply a promise to pay. The important thing is that if such a promise to pay is executed with the necessary formality and then registered, it creates an interest in the real property of the person who has made the promise. This interest is called an hypothec but, for the sake of using a word which is likely to be more familiar to the reader, I will call it a “charge”. However, it should not be confused with a charge under English law.

## How is a charge created?

In order for a bond to constitute a charge over the real property of the debtor it must be:

1. Consented to devant justice. This involves the debtor appearing before a Lieutenant Bailiff and two Jurats of the Royal Court and agreeing to be bound by the provisions of the bond.
2. Registered at the Greffe. The original requirement was simply for a document to be consented to devant justice but a system of registration was introduced so that third parties could ascertain what charges there were against a property. The principal legislation dealing with registration is an Ordinance of 1631 as amended by an Ordinance of 1724.

## What is the effect of the charge?

The effect of registering a bond which has been consented to devant justice so as to constitute a charge is twofold:

1. In the event of saisie proceedings, the creditor under the bond has priority over other creditors of the debtor other than creditors with prior registered charges.
2. The property which is subject to the charge will remain subject to it until the charge has been discharged. This means that, if the debtor becomes the subject of saisie proceedings, even if the property which has been charged has passed into the hands of a third party (by means, for example, of a sale to the third party by the debtor without the charge having been discharged) the property will be available to the holder of the charge in the saisie. This right to follow the property which is the subject of a charge into the hands of third parties is known as the droit de suite. In practice the fact that a property remains subject to a charge until it is released from the charge (or the charge is “vacated” by the creditor) means that real property cannot be sold on an arms-length basis without payment of the sum charged against the property or agreement on the part of the creditor that he will accept less than

the full sum due, as the purchaser of the property will not wish to acquire it subject to a charge given to secure the seller's debt.

### Is there any other way of charging real property?

If judgment against the debtor is obtained and then registered at the Greffe, the effect of registration is to create a charge over the real property of the debtor.

There have been attempts to get around the need to enforce a charge against real property by means of saisie proceedings (which, as we will see, take some time to complete) by vesting real property in a company and having the company placed within the control of the lender, so that, upon default in repayment of the debt, the company could sell the property and use the proceeds of sale in payment of the debt due by the debtor. Such a structure was considered by the Guernsey Court of Appeal in *Gaudion v Weardale Limited*. The court stated that:

“If security is to be taken over realty in Guernsey, that security must be taken in the usual way by bond and must be registered..... In the absence of these formalities, the taking of security over land by manipulation through corporate ownership..... would lend itself to the oppression of impecunious debtors.”

The court did, however, go on to say that it would be possible to create security over the shares of a company which owned real property by means of a security agreement which met with the requirements for the taking of security over shares in a company laid down by the Security Interests (Guernsey) Law, 1993. Generally, however, this is a dangerous area and should be approached with great caution.

### What property is charged by a bond?

All real property which is owned by a debtor when a bond is registered (including property acquired on the same day) is caught by the charge. It is often said that property acquired after the date on which a bond is registered is not caught by a charge. That is not correct. It is stated above that the effect of a charge is to create priority over other creditors and to give the creditor the right to follow the property into the hands of third parties. With regard to property which is acquired after the date of the charge, the charge has the first of these effects, but not the second. In other words, if a person consents to a charge and is then the subject of saisie proceedings, all of the real property which he owns at the date on which the proceedings commence will be caught by the charge. However, a lender cannot rely on property acquired after the date of its charge for security, as the property can be sold by the borrower free from the charge. A lender which wishes to have a first charge over property must ensure that all charges before its own have been discharged or, alternatively, that the holders of those charges grant priority to the lender, even where the charges were registered before the borrower acquired the property over which security is sought.

### Transfers between co-owners and joint owners

Problems often arise in practice in a situation where two people (usually married to one another) own property which was purchased with a loan from a bank on the security of a charge given by both of them over the property. If they fall out they will often agree that one of them will transfer his or her interest in the property to the other on the basis that the one who is to become the sole owner will be solely responsible for further payments in respect of the loan. Normally, the secured lender will be asked to discharge the transferring party from the debt and vacate the charge over the property as against that party. The question arises as to whether, if the lender agrees to the arrangement between the parties in principle, it should require a new bond from the party who will remain indebted.

The answer is that, if the lender relies on the existing bond, there is a risk of the lender losing its security, but the risk is fairly nominal. I will call the party transferring his or her interest S1 and the party to whom the interest is transferred S2. I will assume that S1 and S2 originally own the property “for themselves the survivor of them and the heirs of such survivor” which is by far the commonest method of vesting property in more than one person in Guernsey and which results in the whole of the property vesting in the survivor of the owners on the death of the first of them to die. The risk arises as follows:

1. Whilst S2 remains alive the bank's security is sound. Although theoretically the interest transferred to S2 by S1 is “after acquired” property (because it was acquired by S2 after the date of the bond) and is not therefore subject to the droit de suite (the right to follow it into the hands of third parties, referred to above) in practice it cannot be sold separately from the interest originally acquired by S2 when the property was purchased, which is not “after acquired” and therefore remains subject to the droit de suite.

2. If S2 dies before S1, the property will pass to the heirs of S2. Had it remained as originally vested, it would have passed automatically to S1 by virtue of being vested in S1 and S2 "for themselves the survivor of them and the heirs of such survivor".
3. The heirs of S2 can say that their inheritance results entirely from the transfer of the interest of S1 to S2. Had that transfer not taken place then the heirs would have received nothing on the death of S2; the property would have vested in S1. They can therefore argue that the property which they then own is "after acquired" property for the purposes of the bond (on the basis that what they have acquired results from the transfer, after the date of the bond, from S1 to S2) and can be sold free from the charge created by the registration of the bond.

I should stress that this perceived risk appears never to have caused a problem in practice. Different lenders take different views as to the need to take a new bond from S2 when he or she has the interest of S1 in the relevant property transferred into his or her name. The risk to the bank becomes almost non-existent where the bank has taken security over a life assurance policy on the life of S2 (as will often be the case) such that, when S2 dies, any indebtedness to the bank is paid out of the policy proceeds. The risk is then in effect reduced to a risk that the insurer does not pay out. The only circumstances in which this is likely to occur are if (1) there was material non-disclosure (of a pre-existing medical complaint, for example) on the part of S2 when the policy proposal was completed or (2) S2 commits suicide.

It is worth noting that the potential problem outlined above does not arise unless the lender vacates the original bond as against one of the original parties to it. If the bank does not vacate, or otherwise release the property from its charge, the charge will remain in force.

### General saisie procedure

Saisie (also known as *renonciation par loi outrée*) is the procedure whereby a creditor can have the property of his debtor vested in him in satisfaction of his debt. The procedure has developed over several hundred years. It was modified following an enquiry by Royal Commissioners in the early part of the 19th century. A number of further modifications were effected throughout the 19th century. The procedure was then revised by the Saisie Procedure (Simplification) (Bailiwick) Order 1952. It has not changed significantly since then. Indeed, whilst the 1952 Order has changed the procedure, the substantive law on this subject has not changed. The principal authority in relation to saisie remains the "*Traité de la renonciation par loi outrée*" written by Advocate James Gallienne and published in 1845.

Norman customary law, on which much of Guernsey law is based, always set great store by the ownership of real property. For that reason, the saisie procedure was deliberately lengthy, to give the debtor the maximum possible opportunity to pay off his debts and keep his real property. Typically, in the 19th century, a saisie could take several years to complete. The alterations in the procedure made by the 1952 Order mean that a saisie can now normally be completed within six months.

The procedure has three stages:-

Preliminary Vesting Order;

Interim Vesting Order; and

Final Vesting Order.

### Preliminary Vesting Order

If judgment is taken against a debtor in the Royal Court, the advocate acting for the creditor can ask for permission to levy execution on the real property of the defendant. The grant of this request by the Court (which is automatic) constitutes a preliminary vesting order. It should be noted that, once a creditor has chosen to obtain a preliminary vesting order, that creditor cannot then proceed against the debtor's personal property for the debt. If the debtor has personal property, it is therefore sensible to obtain an ordinary judgment, proceed against the personal property first and then, once the personal property has been exhausted, convert the judgment to a preliminary vesting order, which can be done by a separate application to the Court.

A creditor who has had a preliminary vesting order granted in his favour (whom I will call the "principal creditor") can let the property which is the subject of the order, and carry out repairs to it. If the property is already tenanted, the principal creditor can require the rent to be paid to him. If the debtor is living at the property, it is normal at this stage to institute eviction proceedings against the debtor. The Court has power to stay the proceedings for a maximum of six months and, in practice, that is the stay which is normally awarded.

The debtor remains the owner of the property at this stage and can sell it provided either (1) that the proceeds of sale are sufficient to pay all the creditors with charges against the property or (2) that those creditors agree to take less than the full amount to which they are entitled.

Before moving on to the next stage, the interim vesting order, the principal creditor must arrange a meeting before a Commissioner of the Court, to which the debtor must be summoned, and at which an account is produced which sets out the amount of the judgment obtained by the creditor together with accrued interest and costs. The Commissioner certifies the amount due to the creditor.

### Interim vesting order

The principal creditor summons the debtor to Court to require him to pay the sum due to the creditor as certified in the Commissioner's report. If that sum is not paid, the principal creditor applies for an interim vesting order. If that order is granted, the debtor loses ownership of the property. For that reason, the debtor is given the opportunity to apply to the Court for a stay of the interim vesting order. A stay will be granted, for example, if the debtor can convince the Court that there is "equity" in the property and that he or she will be able to sell it within a reasonably short period of time.

From the date on which an interim vesting order is granted until the date on which a final vesting order is granted, the principal creditor holds the property as trustee for all of the creditors of the debtor. Any rent which he receives from that date must be accounted for.

Having obtained an interim vesting order, the principal creditor opens a register of claims at the Greffe and must give notice in La Gazette Officielle that the register has been opened. The register is open for 28 business days. Any creditor of the debtor (whether or not he has a charge over the property) can enter his claim on the register.

### Final Vesting Order

Once the register is closed, the principal creditor can apply immediately to the Court for an order that the premises be vested in the principal creditor. If this is done, then the principal creditor will be responsible for paying all of the other creditors who have registered their claims at the Greffe. In practice, this procedure is only adopted where no significant claims have been registered at the Greffe other than that of the principal creditor.

Where this procedure is not adopted, the principal creditor must summon all of the creditors who have registered their claims at the Greffe to a meeting before a Commissioner of the Court. The claims of the creditors are then "marshalled"; that is, they are placed in order of priority. Obviously, creditors with charges will be ranked according to when their charges were registered. There is some doubt as to how unsecured creditors rank as between one another. One school of thought has it that they will rank equally ("en parité de droits"). Another has it that they rank according to the date on which they registered their claims at the Greffe.

After the marshalling of claims, the Commissioner appoints a date at which the proceedings will be terminated, being the date of a Plaid d'Heritage sitting of the Royal Court. At that sitting the principal creditor summons each creditor, in reverse order of priority, either to elect to have the property which is the subject of the saisie vested in him or to renounce his claim. A creditor who, when the property is offered to him, declines to take it, is deemed to have renounced to his right so to do and his claim ceases to be of any effect. A creditor who takes the property has a final vesting order made in his favour, the effect of which is to vest the property in that creditor absolutely. He must pay all creditors whose registries rank ahead of his in full within fifteen days. The creditor who takes the property is under no obligation to sell it. If, however, he does sell it, he is under no obligation to pay any surplus proceeds of sale over and above the amount of the debt due to him either to the debtor or to any creditors of the debtor. In the case of *Gaudion -v- Weardale Limited* the Guernsey Court of Appeal described the fact that a creditor who obtains a final vesting order and sells property at a price which exceeds the amount of the debt may retain the surplus as "a relic of ancient Guernsey customary law, which in [the Court's] judgment would well bear reconsideration by the relevant authorities. They may consider that at the end of this 20th century it would be appropriate for any surplus to go to the impoverished debtor rather than as a windfall to the relevant creditor."

There are a number of matters to note in relation to the saisie procedure:

### General and specific charges

A saisie relates to all of the real property of the debtor. A creditor cannot choose to take saisie proceedings in respect of some only of the debtor's real property. This leads to some interesting questions in the context of situations where specific charges have been given or priority has been given by one lender to another in

relation only to one of two or more of a debtor's properties.

Most charges are general charges; they charge all of the property of the debtor. However, where a potential borrower has more than one property, or already owns a property and wishes to acquire another, it is not uncommon for a charge to be created which charges only the property specified. Another fairly common practice is for a bank ("bank 1") to lend on the basis of a general charge and for another bank ("bank 2") which already has a general charge to give priority to bank 1 (in respect of bank 1's charge) over bank 2's charge, but in such a way that the priority is limited to a particular property.

The effect of both of these practices is to create a situation where the properties of a debtor may be subject to different charges, or to the same charges but in different orders of priority. We need to ask ourselves how such a situation would be dealt with in the event of saisie proceedings against the debtor. Remarkably, there appears not to have been a saisie where this question has arisen.

I have little doubt that, should these circumstances arise, the Court would attempt to develop a procedure to take account of the intentions of the parties. However, this is not as easy as it might seem. The obvious solution is to have a separate marshalling of claims and separate final vesting order proceedings in relation to each property. However, let us take for example a situation where there are two properties; property 1 and property 2. Both properties are the subject of a general charge, which is a first charge, in favour of bank A. Property 1 is the subject of a second charge in favour of bank B and property 2 is the subject of a second charge in favour of bank C. No one other than these parties registers a claim in the saisie register opened following the grant of an interim vesting order. If there is a separate marshalling of claims in respect of each property bank A will be at the top of both lists. If there are then separate final vesting order proceedings property 1 will be offered to bank B subject to paying off bank A and property 2 will be offered to bank C subject to paying off bank A. How can this work? Does bank A get paid twice? Obviously not. One set of final vesting order proceedings would have to precede the other. If the proceedings in respect of property 1 are before those in respect of property 2 does bank B have to pay bank A in full in order to have property 1 vested in it, leaving bank C with nothing to pay bank A in the proceedings relating to property 2? Again, obviously not.

It is difficult to see how, in the example given above, having two marshallings of claims and two final vesting order proceedings could work. However, it is also difficult to see what the alternative would be.

## Guarantees

Particular care needs to be taken where security for lending comprises a charge from a principal debtor backed up by a guarantee. It is certainly arguable that, if saisie proceedings are taken against the principal and the creditor has the principal's real property vested in it, then that vesting will be taken as satisfaction of the principal debt, leaving no debt to be claimed under the guarantee. In the only case that has come before the Court on this matter, (*The Liquidators of the Late Shopper Limited -v- Barclays Bank Plc*) the Royal Court held that a claim could be made under the guarantee notwithstanding that saisie proceedings had been taken against the principal which had culminated in his real property being vested in Barclays Bank. The question is, however, by no means beyond doubt. If we take the reverse situation, where saisie proceedings are taken against a guarantor and the guarantor's property is taken by a creditor, the question arises as to whether proceedings can then be taken against the principal by that creditor for the recovery of the balance. It is submitted that they can, on the basis that nothing other than payment in full can discharge the principal debt.

In the light of these doubts which exist in relation to guarantees, the sensible course of action to take is only to claim against each of the principal and the guarantor the amount which it is expected to realise from that particular party. There is no doubt that the balance can then be claimed from the other party.

## Conclusion

The saisie system is certainly an interesting one and a part of Guernsey's history which makes the island's legal system distinctive from others. Whether it ought to be the system which continues to govern the realisation of security over real property is perhaps more doubtful. In the Edwards Report, a review of financial regulation in the Channel Islands and the Isle of Man, commissioned by the United Kingdom Home Office and published in 1998, it was suggested that Guernsey should review its insolvency laws, and it may be that the saisie system will be a victim of that review. Having said this, the Royal Commissioners who reviewed the system in the first part of the 19th century suggested that it be fundamentally altered, and we still have it more than 150 years later.

## RIDER

This paper is intended as a general review and aide memoire. It does not create a retainer or lawyer-client relationship and does not provide comprehensive or specific legal advice concerning the matters contained within it. This paper should not be relied upon as giving or providing advice on any individual case.