

BLUNDELL LECTURES – 34<sup>TH</sup> ANNUAL SERIES

THE ENFORCEABILITY AND UNENFORCEABILITY OF CHARGES OVER

LAND – PART I

HAVE I GOT A CHARGE?

Introduction

1. The overriding theme of this year's Blundell Lectures is dictated by the economy. Do I have to pay? Can I get out of paying? Can I sue the guarantor? These are the questions which last came to prominence in the property crash of the early nineties. They have returned, in a more virulent form. The deal driven cases which were still crossing my desk this time last year have gone, to be replaced by clients seeking exit routes from conditional contracts negotiated in better times, clients seeking to activate or frustrate break clauses, clients seeking to stave off lenders or enforce securities, and a myriad of other cases driven by the contraction in credit and the contraction in the economy.
  - 1.1 Standing at the centre of all this is the mortgage market, both residential and commercial. In the first blast of the recession my impression has been that lenders have preferred to avoid or defer the enforcement of their securities, perhaps on the basis that enforcement at the bottom of the market is not the best option.
  - 1.2 It is difficult to believe that this state of affairs will last. Whatever politicians may say about green shoots, past experience of recessions tells us that after a certain period of time debtors run out of money and excuses, and lenders run out of patience. It is at that point that lenders look to enforce their securities, and it is at that point that everyone starts to look very closely at the security agreement entered into in better times.

- 1.3 In tonight's lecture the task which Carol and I are undertaking is to carry out at least part of that scrutiny, in relation to charges over land, before the balloon goes up for those of your clients who may be looking to enforce or to resist the enforcement of a charge over land.

#### Enforcing charges – the basic questions

2. The question of whether a charge over land is enforceable or unenforceable can be recast into some more basic questions.
  - 2.1 First, have I got a charge over land? What formalities must be observed for its creation? What kind of charge have I got?
  - 2.2 Second, if I have got a charge, can I enforce it? How do I enforce the charge? What remedies can I obtain? Have I waited too long to enforce?
  - 2.3 In these two lectures I will be dealing with the first set of questions. Carol will deal with the second set of questions.

#### What is a charge over land?

3. The terms mortgage and charge are used pretty much interchangeably these days, at least where land is concerned. They are however conceptually different. The history of mortgage law is a subject strictly for property law anoraks, but it is worth knowing that the essential nature of a mortgage of land is that it is a conveyance of a legal or equitable interest in land, with a provision for redemption. Reference to the provision for redemption means that, upon repayment of the loan secured by the mortgage, or upon the performance of some other obligation, the conveyance becomes void or the interest is reconveyed.
  - 3.1 A charge of land is not a conveyance. A charge over the land is the appropriation of an interest in land for the discharge of a debt or other obligation, without the creditor having either a general or a specific property in, or possession of the land.

- 3.2 Section 87(1) of the Law of Property Act 1925 introduced a new species of charge known as the charge by deed expressed to be by way of a legal mortgage. This is also referred to as a legal charge. A legal charge is essentially a statutory form of legal mortgage. Under such a statutory form of legal mortgage there is no conveyance of any estate to the mortgagee, but the chargee has the same protection, powers and remedies as if a mortgage by demise had been made.
- 3.3 So far as a legal charge is concerned, the formalities are fairly straightforward. It is in relation to equitable charges that the position becomes more complicated. It is for this reason that the essential nature of a charge is described at the outset of this lecture. The circumstances in which an interest in land may be said to have been appropriated for the discharge of a debt or other obligation are many and varied.

Do I need a piece of paper to have a charge over land?

4. Where a legal charge is concerned, the answer is an unequivocal yes. A legal charge must be made by deed; see Section 52 of the Law of Property Act 1925. Section 52 applies to conveyances, but the definition of a conveyance in Section 205 of the 1925 Act includes a charge.
- 4.1 In the case of registered land Section 23 of the Land Registration Act 2002 gives the owner of a registered estate in land the power enter into a charge by way of legal mortgage of the registered estate or, more simply, to charge the registered estate with the payment of money. Section 24 of the 2002 Act identifies the owner as the registered proprietor of the registered estate or the person entitled to be so registered as the proprietor. Whichever method of charging the land is used, the relevant charge will not take effect as a legal charge until it has been registered against the relevant estate; see Section 27 of the 2002 Act. Section 51 of the 2002 Act further provides that, on completion of the relevant registration requirements, a charge created by means of a registrable disposition of a registered estate has effect, if it would not otherwise do so, as a charge by deed by way of legal mortgage. In the case of unregistered land, registration as a land charge will be required under the Land

Charges Act 1972 if the charge falls into any of the categories of land charges set out in Section 2 of the 1972 Act.

- 4.2 In the case of equitable charges the answer to the question, do I need a piece of paper, remains yes, but the position is not quite the same. An equitable charge can only be created in writing, signed by the chargor or his agent; see Section 53(1)(c) of the Law of Property Act 1925. In the case of unregistered land the equitable charge must be protected as a C(iii) land charge within Section 2(4) of the Land Charges Act 1972. In the case of registered land the equitable charge must be protected by the entry of an agreed or unilateral notice against the registered estate in the land affected by the equitable charge.
- 4.3 A contract to create an equitable charge can take effect as an equitable charge, but here a further difficulty intrudes. Such a contract must comply with the requirements of Section 2 of the Law of Property (Miscellaneous Provisions) Act 1989. This means a written document or an exchange of documents incorporating all of the terms of the contract signed by or on behalf of both parties. Indeed it is for this reason that the good old days of creating a mortgage or charge by deposit of title deeds are well and truly behind us; see United Bank of Kuwait v Sahib [1997] Ch 107, as upheld in the Court of Appeal under the same reference. As Chadwick J., as he then was, pointed out in his judgment at first instance in that case, the basis of the creation of a mortgage or charge by the deposit of title deeds was contractual. As such this method of creating a security, by the deposit of title deeds, was caught and rendered void by Section 2 of the 1989 Act.
- 4.4 In the absence of a piece of paper the options available to a party trying to claim an equitable charge over land are limited. It may be that such a charge can be claimed by means of a resulting, implied or constructive trust. There is also the possibility of claiming such a charge on the basis of proprietary estoppel. Neither trust nor estoppel is an easy route. A claim to an equitable charge on the basis of trust or estoppel, particularly in the commercial context, is likely to run into the sort of difficulties which did for the claimant in Cobbe v Yeoman's Row Management Ltd [2008] 1 WLR 1752. A full examination

of this case, and its implications for the doctrine of proprietary estoppel is the subject matter of another lecture in this years series of Blundells Lectures. It is however worth looking briefly at Cobbe for the purpose of this lecture.

4.5 It will be recalled that, in Cobbe, the claimant, an experienced property developer orally agreed with the third defendant to purchase for £12 million a property comprising a number of flats for redevelopment into six town houses. The claimant then spent some 18 months expending considerable time and expense in obtaining planning permission for the redevelopment. Once the planning permission had been obtained the inevitable happened and the defendants withdrew from the oral agreement. The claimant claimed to be entitled to a beneficial interest in the property on the basis of proprietary estoppel and constructive trust. At first instance the claims in proprietary estoppel and constructive trust succeeded, and the claimant was awarded a lien over the property, securing to the claimant one half of the increase in the value of the property brought about by the planning permission. The defendants' appeal to the Court of Appeal was dismissed, but an appeal to the House of Lords was successful. The House of Lords overturned the decision at first instance, and awarded the claimant only a quantum meruit in respect of the money and services which he had provided.

4.6 A full discussion of the decision in Cobbe, and the subsequent decision of the House of Lords in Thorne v Major [2009] 1 WLR 776 is beyond the scope of this lecture. For present purposes I suggest that there are two important points to note for those seeking to construct an equitable charge without the right piece of paper, or indeed any piece of paper. First, the claim in Cobbe failed because the claimant was unable to point to any legal right which the defendants were estopped from asserting. The parties had chosen to work together without the benefit of an enforceable contract. It was understood on both sides that there was no enforceable agreement, and that the full terms of such an agreement remained to be worked out between the parties. This was a gap which could not be filled, either by estoppel or by constructive trust. There was no enforceable right which Mr. Cobbe, encouraged by the defendants, believed himself to have. Second, it was suggested, by Lord Scott

in Cobbe, that proprietary estoppel, which is not specifically exempted from Section 2 of the 1989 Act, cannot be used as a device to render enforceable an agreement which is void by virtue of Section 2. Whether this is the law however, has yet to be established.

- 4.7 The lesson for those seeking to assert an equitable charge without a piece of paper is, I suggest, this. The law of estoppel is only likely to assist if the person asserting the equitable charge is able to say that he believed himself to have an enforceable legal right against another party, with the knowledge and encouragement of that other party, in such a way as to raise an equity which it is appropriate to satisfy by the creation of an equitable charge.
- 4.8 Finally, charges over land given by companies require to be registered in the companies register. Failure to do this will result in the charge being void against a liquidator or administrator or creditor of the company. As from 1<sup>st</sup> October 2009, as currently advised, the relevant provisions will be found in Part 25 of the Companies Act 2006. Pending the coming into force of this new regime, the relevant provisions are to be found in Part XII of the Companies Act 1985.

If I have a piece of paper, is the writing valid?

5. There are all sorts of things which can go wrong with the drafting of a charge document, but I pick out two particular areas where, for reasons which are not obvious, things can go wrong.
  - 5.1 The first area concerns a clog on the equity of redemption. Like me, a clog on the equity of redemption may be something that you remember only very dimly from the mortgages week in your university or law school course. In recent years however there have been a couple of cases which have brought this somewhat arcane area of the law to unexpected light.
  - 5.2 In order to understand a clog on the equity of redemption it is necessary to go back to first principles. A mortgage is a conveyance of land as a security for the payment of a debt or the discharge of some other obligation for which the

mortgage is given. It is fundamental to the notion of a mortgage that it can be redeemed on payment of the relevant debt or discharge of the relevant obligation. So too in the case of a charge. Historically, equity has protected the right to redeem. The modern law is stated in the speeches in the House of Lords in Kreglinger v New Patagonia Meat and Cold Storage Company Limited [1914] AC 25. The expression, clog on the equity of redemption, is used as a generic term to describe what are, in essence, three separate rules.

- (1) A condition in a mortgage or charge which is repugnant to the contractual right to redeem and the equitable right to redeem is void.
- (2) A condition in a mortgage or charge which imposes a penalty in respect of the exercise of the equitable right to redeem, following a failure to exercise a contractual right to redeem, is void in equity.
- (3) A provision in a mortgage or charge which regulates or controls the right to redeem is invalid, if it is unconscionable.

5.3 These rules apply to mortgages and other security interests. It is therefore necessary for the Court, when confronted with the argument that a term in an agreement is void as being in breach of the above rules, to stand back and consider whether the transaction is, in truth, a security transaction; see Welsh Development Agency v Export Finance Co. Ltd [1992] BCC 270. If not, the rules do not apply.

5.4 The topicality of these rules has recently been demonstrated in a decision of Morgan J. in Brighton and Hove City Council v Audus [2009] EWHC 340. In this case the claimant council granted a long lease of a flat to the defendant's aunt and her husband pursuant to the right to buy legislation. The discounted purchase price was provided by the defendant, secured by a first legal charge over the long lease in favour of the defendant. On the same date a supplemental legal charge was entered into between the defendant and the tenants under the long lease, the defendant's aunt and her husband, which secured the payment to the defendant, on redemption of the first charge, of any increase in the value of the long lease between the date of the first charge and the date of redemption.

- 5.5 Subsequently the claimant council registered a third charge against the long lease pursuant to Section 22 of the Health and Social Services Act 1983. The value in this third charge was, obviously, substantially reduced by the presence of the second charge securing the uplift in the value of the flat. The claimant accepted that the first charge was a valid charge with priority to its charge. The claimant also contended however that the second charge was invalid as a clog on the equity of redemption in relation to the first charge. If this argument was correct, the claimant's third charge could thus replace the defendant's second charge as the charge having priority after the first legal charge.
- 5.6 The claimant's argument failed before Morgan J. Looking at the overall substance of the transactions between the defendant and his aunt and her husband, the Judge was satisfied that the composite transaction, as he characterised it, went beyond a security transaction, and was in substance a transaction whereby the defendant would buy the flat and have ownership of the flat, while his rights were to be postponed to the rights of the aunt and her husband to live in the flat for their lives. As such there was no clog on the equity of redemption, or more accurately there was no breach of the equitable rules such as would permit the second charge to be declared void.
- 5.7 In adopting the approach of looking at the overall substance of the transaction the Judge placed considerable reliance upon the judgment of Jonathan Parker LJ in Warnborough Limited v Garmite [2003] EWCA Civ 1544. In summary, what happened in that case was as follows. Warnborough sold land to Garmite. The purchase price was left outstanding as payable to Warnborough. Garmite's obligation to pay the purchase price was secured by a mortgage in favour of Warnborough. Garmite also granted Warnborough an option to repurchase the land. The issue was whether that option to repurchase was a clog on the equity of redemption in relation to the mortgage. The Court of Appeal determined that it was necessary to look at the substance of the transaction in order to determine there was a clog. The Court of Appeal were not in a position to do that themselves as the case came before them on a summary judgment application, but Jonathan Parker LJ expressed the view

that it was likely, when the substance of the transaction came to be examined, that it would be found to be one of sale and purchase and not mortgage. This was indeed the view subsequently reached by the trial judge.

- 5.8 The lack of success, in these cases, in the argument that there was a clog on the equity of redemption should not obscure the point that, in examining the validity of any charge, an important consideration is whether the equitable rules regarding redemption of the charge have been breached. If they have, the result may be very bad news for the lender.
- 5.9 The second area, which I have selected, where things can go wrong, principally concerns the institutional lender. The area in question concerns the Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999 No. 2083). These regulations replaced a previous set of Consumer Contracts Regulations brought into force in 1994. The 1999 Regulations apply to unfair terms in contracts concluded between a seller or a supplier and a consumer. The Regulations apply to contracts relating to land. Charges are therefore caught by the Regulations if they are entered into between seller/supplier and consumer.
- 5.10 The Regulations apply to contractual terms which have not been individually negotiated. A seller or supplier means any natural or legal person who, in contracts covered by the Regulations, is acting for purposes relating to his trade, business or profession. A consumer means any natural person acting for purposes outside his trade, business or profession.
- 5.11 The Regulations are therefore of considerable importance in relation to residential charges, where an institutional lender lends money to an individual on the security of a charge over that individual's residence. In the residential mortgage market the terms of charges are not usually the subject of individual negotiation. Banks offer their mortgage loans to individuals on standard terms, on a take it or leave it basis.

5.12 When are such terms unfair? The short answer to this question is to be found in paragraph 5(1) of the Regulations, which provides as follows.

*“A contractual term which has not been individually negotiated shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties’ rights and obligations arising under the contract, to the detriment of the consumer.”*

5.13 Schedule 2 to the Regulations then sets out a lengthy list of terms which may be regarded as unfair, although the list is expressed to be indicative and non-exhaustive.

5.14 Guidance in case law as to when terms in contracts will be regarded as unfair is more difficult to find. Some indirect guidance may be found in Director General of Fair Trading v First National Bank plc [2001] UKHL 52. The term in issue in that case was a term in a consumer credit agreement, rather than a charge over land, and arose under the former 1994 Regulations. The term in question was a term in the agreement which required the borrower, in the event of default on his payments, to continue to pay interest at the contractual rate until any judgment obtained by the bank was satisfied. The Court of Appeal held that this term was unfair, but the House of Lords disagreed. In the view of their Lordships the term was not unfair in that it essentially did no more than require that contractual interest be paid on a debt. This was part of the bargain pursuant to which the bank made funds available to the customer, to be repaid over a period of time with interest. This was not inherently unfair.

5.15 The reach of the 1999 Regulations is necessarily fairly limited. The relevant term in a charge over land, if it is to be struck down by the Regulations, must be one which creates a significant imbalance between lender and customer. As a general guide I venture to suggest that this means a term in the charge which is both outside the scope of what might be called the original bargain between lender and customer and is significantly weighted in the lender’s favour.

If I have a piece of paper, how did the chargors' signatures get there?

6. In a normal transaction a chargor agrees to execute a charge in order to obtain a loan on the security of the land which is to be subject to the charge. It may be a misnomer to describe the chargor as a willing charger. No one willingly charges land, in the sense that no one would offer land as security for a loan if the loan could be obtained without providing that security. The chargor is however acting of his own free will, in the sense that it is his decision to enter into the charge.
- 6.1 As the recession of the early nineties demonstrated however, an apparently valid charge may be vitiated by the circumstances in which a relevant signature to the charge was procured. Specifically, equity sets a limit to the influence which may be exerted by one party over another in order to obtain the agreement of a party to enter into a charge. Conduct which goes beyond this limit is known as undue influence, and is one of the grounds of relief developed by the courts of equity as a court of conscience.
- 6.2 All kinds of conduct may amount to undue influence. In broad terms however there are two forms of conduct which amount to undue influence. The first comprises overt acts of improper pressure or coercion such as unlawful threats. The second form arises out of a relationship between two persons where one has acquired over another a measure of influence, or ascendancy, of which the ascendant person then takes unfair advantage.
- 6.3 It is the second category of conduct which came to prominence in the last recession, principally but by no means exclusively in cases where wives had entered into security transactions to guarantee the debts of their husbands' businesses. In a typical case a wife would have executed a joint charge with her husband over the jointly owned matrimonial home in order to guarantee the borrowing of the husband or the husband's business. In such a case, proof that the wife reposed trust and confidence in her husband, coupled with a transaction which calls for explanation will raise the evidential presumption that the transaction was procured by the undue influence of the husband.

- 6.4 Why should this matter to the bank lender, the grantee of the relevant security? The bank will not have been the party exercising the undue influence. Why should the security transaction be set aside as against the bank? The answer to these questions is to be found in the decision of the House of Lords in Barclays Bank v O'Brien [1994] 1 AC 180. In this case the House of Lords decided that a wife whose consent to a security transaction had been procured by the legal or equitable wrong of the husband was entitled to have the transaction set aside as against the bank in circumstances where the bank had actual or constructive notice of the legal or equitable wrong. The case was actually concerned with a misrepresentation by the husband, but the principles established by that case apply equally to cases of undue influence or other legal or equitable wrong. Such constructive notice arises where the bank is put on inquiry as to whether the consent of the wife to the relevant transaction has been properly obtained. Lord Browne-Wilkinson determined that a bank is put on inquiry when a wife offers to stand surety for her husband's debts by the combination of two factors. First, the transaction is on its face not to the financial advantage of the wife. Second, there is a substantial risk in transactions of this kind that, in procuring the wife to act as surety, the husband has committed a legal or equitable wrong that entitles the wife to set aside the transaction. The same principle applies in any case where one party offers to provide security for the debts of another party in circumstances, where, to the knowledge of the bank, the parties are in what might be described as partnership relationship, whether heterosexual or homosexual. Where the bank is put on inquiry, and the relevant consent has been obtained by undue influence or some other legal or equitable wrong, the bank will be fixed with constructive notice of the undue influence or other legal or equitable wrong unless it takes steps to satisfy itself that the relevant consent was properly obtained.
- 6.5 Returning to the subject matter of this lecture, the critical question for the grantee of a charge given in circumstances analogous to the O'Brien case is what to do when put on inquiry of the possibility of undue influence or some other legal or equitable wrong.

6.6 The answer to this question, so far as cases emerging from the current recession are concerned, is to be found in the decision of the House of Lords in Royal Bank of Scotland plc v Etridge (No. 2) [2002] 2 AC 773. In his speech in that case Lord Nicholls provided a comprehensive guide to this area of the law and, in particular, set out the steps, for the future, to be taken by a bank in order to avoid being fixed with constructive notice that the consent of a third party to its security was procured by a legal or equitable wrong.

6.7 Lord Nicholls stated that the furthest a bank can be expected to go, in order to avoid being put on inquiry, is to take reasonable steps to satisfy itself that the wife or other third party in an analogous position has had brought home to her, or him, in a meaningful way, the practical implications of the proposed transaction. What is meant by reasonable steps? Lord Nicholls put the matter this way, at paragraph 50 of his speech.

*“For the future a bank satisfies these requirements if it insists that the wife attend a private meeting with a representative of the bank at which she is told of the extent of her liability as surety, warned of the risks she is running and urged to take independent legal advice. In exceptional cases the bank, to be safe, has to insist that the wife is separately advised.”*

6.8 Lord Nicholls acknowledged that banks do not often follow this course, and do not like to follow this course, because of the risk of things being said or being alleged to have been said in the meeting which compromise a subsequent claim on the security. Lord Nicholls confirmed that the task of explaining the implications of the transaction to the wife or other third party could be entrusted to a solicitor acting for the wife or other third party. If the bank selects this option the steps which the bank must take were identified by Lord Nicholls, at paragraphs 79 and 80 of his speech, in the following terms.

*“79 I now return to the steps a bank should take when it has been put on inquiry and for its protection is looking to the fact that the wife has been advised independently by a solicitor.*

*(1) One of the unsatisfactory features in some of the cases is the late stage at which the wife first became involved in the transaction. In*

*practice she had no opportunity to express a view on the identity of the solicitor who advised her. She did not even know that the purpose for which the solicitor was giving her advice was to enable him to send, on her behalf, the protective confirmation sought by the bank. Usually the solicitor acted for both husband and wife.*

*Since the bank is looking for its protection to legal advice given to the wife by a solicitor who, in this respect, is acting solely for her, I consider the bank should take steps to check directly with the wife the name of the solicitor she wishes to act for her. To this end, in future the bank should communicate directly with the wife, informing her that for its own protection it will require written confirmation from a solicitor, acting for her, to the effect that the solicitor has fully explained to her the nature of the documents and the practical implications they will have for her. She should be told that the purpose of this requirement is that thereafter she should not be able to dispute she is legally bound by the documents once she has signed them. She should be asked to nominate a solicitor whom she is willing to instruct to advise her, separately from her husband, and act for her in giving the necessary confirmation to the bank. She should be told that, if she wishes, the solicitor may be the same solicitor as is acting for her husband in the transaction. If a solicitor is already acting for the husband and the wife, she should be asked whether she would prefer that a different solicitor should act for her regarding the bank's requirement for confirmation from a solicitor.*

*The bank should not proceed with the transaction until it has received an appropriate response directly from the wife.*

*(2) Representatives of the bank are likely to have a much better picture of the husband's financial affairs than the solicitor. If the bank is not willing to undertake the task of explanation itself, the bank must provide the solicitor with the financial information he needs for this purpose. Accordingly it should become routine practice for banks, if relying on confirmation from a solicitor for their protection, to send to the solicitor the necessary financial information. What is required must depend on the facts of the case.*

*Ordinarily this will include information on the purpose for which the proposed new facility has been requested, the current amount of the husband's indebtedness, the amount of his current overdraft facility, and the amount and terms of any new facility. If the bank's request for security arose from a written application by the husband for a facility, a copy of the application should be sent to the solicitor. The bank will, of course, need first to obtain the consent of its customer to this circulation of confidential information. If this consent is not forthcoming the transaction will not be able to proceed.*

*(3) Exceptionally there may be a case where the bank believes or suspects that the wife has been misled by her husband or is not entering into the transaction of her own free will. If such a case occurs the bank must inform the wife's solicitors of the facts giving rise to its belief or suspicion.*

*(4) The bank should in every case obtain from the wife's solicitor a written confirmation to the effect mentioned above.*

80 *These steps will be applicable to future transactions. In respect of past transactions, the bank will ordinarily be regarded as having discharged its obligations if a solicitor who was acting for the wife in the transaction gave the bank confirmation to the effect that he had brought home to the wife the risks she was running by standing as surety."*

6.9 For a recent example of a case involving undue influence I refer you to the recent decision of Lewison J. in Thompson v Foy [2009] EWHC 1076 (Ch). The case is of particular interest because the relevant allegation of undue influence failed. The Judge found that the kind of trust in play in the case was no more than the trust of a mother that a daughter would keep her promise to her mother. Even if undue influence had been established against the daughter it would not have permitted the mother to set aside a charge over the property because the undue influence which was alleged would not, if it had been established, have occurred until after the grant of the charge.

If I have a piece of paper, in the right form, and with the right registrations, and with the right procedures followed to avoid constructive notice of a legal or equitable wrong, what can possibly go wrong?

7. I have included this last question because one thing which can go wrong, even if everything to do with a registered charge looks secure, is rectification of the register. Since the last property recession the law of land registration has been subject to significant changes. We now have the Land Registration Act 2002, in place of the Land Registration Act 1925. Among the many changes made by the new 2002 Act is a new regime for alteration of the register in the circumstances set out in Schedule 4 to the 2002 Act. Where such alteration involves the correction of a mistake and prejudicially affects the title of a registered proprietor, such alteration is known as rectification.

7.1 A full explanation of the way in which the new regime works is beyond the scope of this lecture. I do however want to put before you two examples of the operation of the new law of rectification, which illustrate some differences between the old and new regimes.

7.2 A problem which can face a secured lender is not any problem with his own charge, but rather a problem with the title being charged. I refer specifically to a case where the person charging the relevant land has acquired the title by a void disposition. The classic instance of this as follows. R1 is the registered proprietor of land. R2 forges the signature of R1 on a transfer of the land to R2. R2 then charges the land to a bank as security for a loan. Subsequent to the granting of the charge the fraud is discovered. R1 seeks rectification against R2, so that R2 is removed from the registered title and replaced by R1. This is not a problem. A mistake has occurred which can be rectified pursuant to the provisions of paragraph 2 of Schedule 4 to the 2002 Act. A party in possession of land may be able to resist an order for such rectification provided that he has not caused or contributed to the mistake which has given rise to the need for rectification, but it will be no answer for R2 to protest that he is in possession of the relevant land since he will, plainly, have caused the mistake by his own fraud.

7.3 What however is the position of the bank, as chargee of the land? Under the old law it was possible for rectification to be made against the chargee in the example set out above. This is however no longer the position. Provided that the bank took its charge from R2 after the registration of R2 as the proprietor of the relevant land, rectification is not available against the bank. The reason for this is that Section 58(1) of the 2002 Act provides that if, on the entry of a person in the register as the proprietor of a legal estate, the legal estate would not otherwise be vested in him, the legal estate is to be deemed to be vested in him as a result of the registration. Thus, in the example given above, R2 had full powers of disposition, in relation to the registered estate, when he granted the charge to the bank. There are therefore no grounds for interfering with the registration of the charge. It was granted by someone who, at the time when the charge was granted and notwithstanding the subsequent removal of R2 from the registered title, was the registered proprietor of the relevant land and had the powers of disposition of a registered proprietor.

7.4 The answer to this, from R1, might be thought to be the argument that the bank's registration of the charge was the result of a mistake, namely the forged transfer, just as much as R2's registration was a mistake. This argument was however firmly rejected in Barclays Bank v Guy [2008] EWCA Civ 452, where the facts were on all fours with the example I have just given. Lord Justice Lloyd stated the position succinctly, at paragraph 23 of his judgment, in the following terms.

*"I simply cannot see how it could be argued that if the purchaser or chargee knows nothing of the problem underlying the intermediate owner's title, that the registration of the charge or sale to the ultimate purchaser or chargee can be said to be a mistake. That seems to me inconsistent with the structure and terms of the 2002 Act."*

7.5 It is however very important to note that rectification would be available against the bank, in the example given above, if the bank took its charge from R2 before R2 was actually registered as proprietor of the land. This could quite easily happen. R2 might procure the forged transfer and execute the legal charge at the same time. Both transfer and legal charge are then

registered. R1 then applies for rectification so as to reinstate himself as proprietor of the relevant land. On these facts R1 will be able to secure rectification against both R2 and the bank.

7.6 This apparently arbitrary difference comes about because, in the second example, R2 did not have the powers of a registered proprietor of the land at the time when he executed the charge. This would not normally be a problem because, in a normal transaction, R2 would have the entitlement to be registered as proprietor of the land. As such, R2 would normally have owner's powers in relation to the registered estate, notwithstanding that he had not actually been registered as the proprietor of the registered estate; see Sections 23 and 24 of the Land Registration Act 2002. The transaction is not however a normal one. In this second example R2 has no entitlement to be registered as proprietor of the land in advance of his actual registration, because the forged transfer was a void disposition. The consequence is that owner's powers were not available pursuant to Section 24 of the 2002 Act, and R2 had no power to charge the land to the bank at the time when he charged the land to the bank. As such the registration of the bank's charge will have been the consequence of a mistake within the meaning of paragraph 2 of Schedule 4 to the 2002 Act, and rectification against the bank is available. This will leave the bank to the vagaries of a claim for indemnity pursuant to the provisions of Schedule 8 to the 2002 Act which is not, as they say, a good place to be.

7.7 The difference between the above two examples, neither of which operates in the same way as under the previous law, does illustrate the extent to which the law has changed as a consequence of the Land Registration Act 2002. The examples also illustrate that, to a greater extent than before, a registered charge should be secure, provided that it is granted by someone who, at the time when he grants the charge, is the registered proprietor of the relevant land. Under the 2002 Act it is the actual fact of registration which is of paramount importance. The lesson of the above examples, for those acting for secured lenders, is a simple one. Be careful in your dealings with those entitled to be registered, as opposed to those actually registered and, whatever

else (outside your control) which may go wrong with the obtaining of a charge, at least make sure that there is no mistake in the registration of the charge.

EDWIN JOHNSON QC

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