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In Practice

Insolvency sales and the community right to buy in Scotland: traps for the unwary

KEY POINTS

- This article will consider the legal and practical issues of the Community Right to Buy regime faced on an insolvency sale of property in Scotland by an insolvency practitioner.
- Introduced in 2004 for rural areas only, the Community Right to Buy (CRTB) now applies to all property in Scotland, urban or rural, subject to limited exceptions.
- The legislation gives an approved community body with a registered CRTB over property a right of first refusal if the landowner or insolvency practitioner wishes to sell it. Any sale to a third party in breach of this legislation would be void.

LAND REFORM AND COMMUNITY ENGAGEMENT: AN OVERVIEW

Land reform and community engagement in land are important policies for the Scottish government which sees land as an asset that should benefit the many rather than the few. Aspirations were announced in 2015 to have one million acres in community ownership by 2020. The CRTB is a key part of this policy as it allows approved community bodies throughout Scotland (including those in large towns and cities) to register an interest in any property (subject to limited exclusions) which leads to an opportunity to purchase that property for the benefit of the local community when it comes up for sale. There are other community rights to buy property in Scotland such as the right to buy abandoned, neglected or detrimental land but these fall outwith the scope of this article.

Before permitting a community body to register an interest, the community body (which must be geographically connected to the property and be a company limited by guarantee, Scottish charitable incorporated organisation or community benefit society) must convince the Scottish Ministers the acquisition of the property is compatible with furthering sustainable development. The Scottish Ministers must also be convinced there is sufficient community support for the registration and that registration is in the public interest.

Having a registered CRTB cannot be used to force a sale on an owner that wishes to retain ownership of the property. However, as long as there is a registered CRTB, the owner of the property or any creditor in a standard security (a Scottish fixed charge) over the property cannot take any steps to sell the property (including marketing) without triggering the right to buy in favour of the community body. Any sale of the property to a third party in contravention of this would be void.

WHY DOES THIS MATTER TO INSOLVENCY PRACTITIONERS?

Value

An insolvency practitioner is concerned with realising assets for a proper price. If there is a registered CRTB affecting the property, the price payable will, in the absence of agreement with the community body, be determined by an independent valuer (normally the District Valuer) on the basis of the market value of the property when the right to buy was triggered. Right of appeal is limited.

Timing and delays

If the right to buy is triggered, a community body has eight months to complete the purchase – a lengthy period for an insolvency practitioner intent on an efficient disposal of an insolvent party's assets. If the community body fails to complete the purchase within this period (subject to permitted extensions), then the right to buy is extinguished and the insolvency practitioner can sell as they wish (subject to the proviso that the community body can apply again for registration of a community right to buy at any point in the future). Given there is no guarantee a community body will be able to raise the finance for the purchase an insolvency practitioner can be left facing a lengthy period of uncertainty.

Not exempt

Sales of property by an insolvency practitioner are not exempt from the community right to buy legislation.

PRACTICAL IMPLICATIONS FOR A SALE

The ability of an insolvency practitioner to dispose of property in Scotland at the price and timescales they wish will depend on whether or not a CRTB has been registered against the property, and if so, when. An early post appointment check should therefore always be made of the Register of Community Interests in Land (RCIL) to see whether a CRTB has been registered against property affected by the insolvency. This is free to inspect and can be found at <http://rcil.ros.gov.uk/>.

If this check finds a CRTB has been registered, the insolvency practitioner may neither sell nor market the property. Instead the insolvency practitioner must before marketing the property give notice to each relevant community body and the Scottish Ministers. This triggers the right to buy and the community body has 30 days

Big box

Susan Gillon is Counsel in Dentons' Glasgow office specialising in advising insolvency practitioners on real estate transactions. She recently advised administrators on the issues set out in the article below. Sarah Peock is a senior practice development lawyer at Dentons based in the Edinburgh office. She supports the Scottish real estate team on technical updates and legal knowhow and has experience of selling land subject to a community right to buy.

to decide if they wish to buy. If they confirm they do wish to buy, the right to buy is activated and they have eight months to complete the purchase at the value set by the independent valuer (with no guarantee they will). Technically a landowner doesn't have to sell at all – it can decide to withdraw the property from sale but as an insolvency practitioner's role is to realise assets and a CRTB Notice lasts for five years (and can be renewed), retaining ownership of the property is unlikely to be a realistic option for an insolvency practitioner.

The CRTB process timetable will also have implications for the duration of any administration appointment as it is likely to take almost a year to dispose of any affected property to a community body and longer to then sell on to a third party if the community body does not complete the purchase.

Even if the check doesn't show a registered CRTB, a sale to a third party is not safe from challenge until after a sale contract or option has been concluded (exchanged). If a CRTB application is made before the contract is concluded but during negotiations then (assuming additional criteria are met by the community body) the CRTB application could be registered and immediately triggered. The insolvency practitioner would then have the uncertainty and delay of the right to buy process with the community body at the price set by the independent valuer (which could be less than an agreed third party price) and would most likely lose the prospect of a shorter term realisation of the asset's value. In addition not every third party purchaser will be prepared to wait and see if the community body fails to complete the purchase.

In light of the CRTB legislation any third party purchaser is likely to insist on being given copies of any CRTB notice received by the insolvency practitioner and insolvency practitioners should ensure copies of any correspondence from the Scottish Ministers or any community body are given to their legal team immediately. The prospective purchaser is also likely to seek confirmation that no CRTB notices have been received by the seller/insolvency practitioner. Even if the purchaser does not insist on this confirmation, it will seek to protect itself by ensuring that delivery of a clear RCIL search is a precondition of completion.

On a more positive note, if a CRTB application is received after a sale contract or option has been concluded with a third party, the Scottish Ministers must decline to consider the application. However, as the Scottish Ministers place a temporary entry on the RCIL while a landowner is being notified of the CRTB application, this means a third party purchaser can't register their title until this entry has been cleared. This is done by the insolvency practitioner providing evidence of the concluded contract or option. Typically sale contracts place an obligation on the insolvency practitioner to do this as soon as possible.

However, a practical difficulty arises if the insolvency practitioner and purchaser wish a simultaneous conclusion and completion of the sale. In this situation, there is a risk a community body may have registered (or applied to register) a CRTB on the date of conclusion of a contract for the sale of the property which would be capable of invalidating the title transfer after the purchaser had paid the

price and otherwise completed the transaction. The risk is relatively small as the process to register a community interest is fairly public. However, the only way to entirely avoid the risk is to complete the transaction the day after the contract is concluded to allow it to be established that the RCIL is clear to the contract date. Any risk the transaction needs to be unravelled after settlement is thereby avoided.

Sometimes simultaneous conclusion and completion remains the preferred route for commercial reasons. If this is the case, in a solvent sale it is usual for the contract to provide for the sale to be unravelled if a community makes a late application to register a CRTB. The parties would be put back into the position they were in before the sale with the purchaser vacating the property and being refunded the price (including any deposit), rates and utilities etc. Any rent received by the purchaser would be set off against any refund.

Insolvency practitioners may try to limit what should be refunded in terms of occupational costs and seek to minimise refunds beyond the price. Furthermore, if the sale also includes the sale of a business, consideration should be given to whether or not any refund/unravelling should relate to the property only or to the whole business (including the property).

In the case of administration as the sale contract would have been entered into by the company post administration, any requirement to refund would be caught by para 99(4) Sch B1 of the Insolvency Act 1986 and classed as an expense of the insolvency and therefore payable at the top of the expense payments waterfall. Given that administrators would be well advised to hold off distributing the sale proceeds to the secured lender (or obtaining an indemnity from the secured creditor for any distributions to cover the insolvency practitioner's fees) and definitely holding off distributing to unsecured creditors any amounts which would not be payable if a reimbursement did have to be made.

Another option involves a staged refund with the price less sums paid to the secured lender being repaid at the outset and the balance being payable (potentially with interest at an agreed rate) when the property is finally sold.

THE POSITION IN ENGLAND

At this time there is no comparable community right to buy in England. There is a community right to bid which allows communities and parish councils to nominate qualifying buildings or land for listing by the local authority as an asset of community value with up to a six months' moratorium on the sale of listed assets to allow the community a chance to raise finance and then make a bid. The English community right to bid is not a community right to buy, just to bid which means a community bid may not be the successful one. Unlike in Scotland, this legislation does not give a first refusal to a community body. However, just as the UK government adopted the Scottish government's introduction of progressive rates for SDLT, it cannot be ruled out that a future UK government may wish to introduce a similar community right to buy for local communities in England. ■