Divergences of Property Law, an Obstacle to the Internal Market?

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1.1 Prologue

The essays collected in this book are based on the contributions presented by the participants of a Leiden University colloquium on September 1st and 2nd, 2005 on the topic ‘Divergences of Property Law, an Obstacle to the Internal Market?’ A summary of the discussions is also included. The essays of the distinguished authors generally treat – as they did during the colloquium – two key questions: Are the divergences in the law on security rights an obstacle to the internal market, and if the divergences are an obstacle, which solutions can solve this problem? In conformity with the colloquium the perspective of the essays is a transnational (comparative and EU-oriented) one.

Both the colloquium and the book follow up the comparative study by Von Bar and Drobnig as published in ‘The Interaction of Contract Law and Tort and Property Law in Europe.’ The background and purpose of this study can be summarised as follows. The EU Commission had decided to use the law of contract as the object of Community action in the form of a so-called Framework of Reference, intended to consolidate and formulate the Community’s “acquis”. As is well known, one major purpose to be achieved is the consolidation and internal harmonisation of the bundle of some Directives on consumer contracts which have been issued since 1985. In addition to

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the task of internal consolidation and harmonisation, an external issue arose, i.e. the potential interaction between a harmonised system of contracts on the one hand and the related fields of property and tort law on the other hand. That was the topic of the study entrusted to Von Bar (as far as it concerns the interaction of contract and tort law) and Drobnig (as far as it concerns the interaction of contract and property law). It soon turned out that the interaction between tort and contract law is much broader and more intensive than that between property and contract law. The dimension of the second part of the study on the relationship between contract and property law was much more modest (less than a quarter of the book). As to substance: it is essentially limited to contractual dispositions of property rights, and specifically to four types of these: the transfer of title in movables, security rights in movables, security rights in immovables (real estate mortgages) and trusts. The colloquium and this book only focus on contractual security rights in movables including the transfer of title of movables.

The study for the EU Commission deals with a relatively narrow, but theoretically interesting point of the interplay between contract law and property law. Furthermore, it illustrates in a very penetrating manner the broad variety of contractual and/or proprietary requirements for giving effect to security rights in movables in the EU. Although it is not the aim of the study, it also shows that this variety has a disastrous effect on the internal market,\(^2\) as pointed out in more detail by Drobnig and Snijders in their contributions. In arranging the colloquium ‘Divergences of Property Law, an obstacle to the internal market?’ we did not want to narrow the discussion to the point of the interplay between contract law and property law. The broader issue is whether the divergences of property law in general and of the rules on proprietary security in particular are obstacles to realising an internal market within the European Union. As we have said before, we asked ourselves two major questions: Are the divergences in the law on security rights an obstacle to the internal market? If the divergences are an obstacle, what solutions can solve this problem? Obviously, these are not simple questions. In this general introduction we give a short overview of the contributions gathered in the colloquium book. At the end of this general introduction, after analysis and discussion of the findings, we try to draw some conclusions from the contributions.

\(^2\) No. 733.
I. Divergences of Property Law, an Obstacle to the Internal Market?

1.2 Summary of the contributions

1.2.1 Transfer and Creation of Property Rights in General

Verstijlen (Groningen) in his contribution discusses general aspects of the creation and transfer of property rights, including security rights. He examines to what extent differences between legal systems for the transfer and creation of property rights in Europe are likely to cause problems in the field of the internal market. As all contributions do, Verstijlen’s contribution concentrates on property rights in movables in particular, since the most urgent problems seem to occur in this area. Verstijlen points out that the legal systems of property law within the EU differ essentially in three respects: whether or not there is a closed list (numerus clausus) of property rights; the requirements for transfer of title (including the distinction between the consensual systems and the systems based on tradition) and whether or not there is a causal link between the underlying contract and the property right (causal and abstract systems). He doubts whether the differences between the various legal systems in the area of the creation and transfer of property rights constitute an obstacle to the internal market, because the playing field throughout the internal market is level for all the players. However, there are obstacles in the internal market. These obstacles lead to increased transaction costs. Verstijlen is in favour of European action to remove these barriers. In his view a ‘Community Security Right’ is the most practical solution. The Community Security Right should consist of a ‘bundle of national security rights, created by one single act’, such as an agreement followed by registration in a public European register.

Håstad (Stockholm) concentrates on the problems of transfer of ownership and distinguishes three issues. The first question is whether the passing of property should require only one agreement or whether such a transfer requires two agreements. The second question is whether the agreement or agreements must be accompanied by an additional disposition to have effect with regard to third parties. The third question is whether there should be a unitary conception of the transfer of property or rather a split approach should be taken dealing separately with different aspects of the passing of property. The author favours the latter approach and on this basis discusses the main issues of the passing of property and describes the problems that arise in case of the seller’s insolvency and the buyer’s insolvency. Invalidity, causal or abstraction principles and bona fide acquisitions are also discussed. Håstad ends his contribution with a reflection on other breaches of contract (which makes the seller interested in terminating the contract and having the goods returned) and a clear rule on conditions and problems to be solved concerning sales for another party and acquisitions for another party.
1.2.2 Effects of Security Rights

The contribution by Steven (Edinburgh) discusses specific divergences in the effect of security rights *inter partes*. Steven divides the creation of conventional security rights into three parts: first, the constitution of the obligation that is to be secured, second, the security contract and third, the creation of the real right in security. The focus in Steven’s contribution is on the second of these issues and therefore the obligations that arise with that contract as a consequence. Steven begins by noting the distinction between true and functional securities, followed by a consideration of how the security contract is created and the obligations that may be secured. He examines the obligations of the parties during the existence of the security and when the security is being enforced. Steven shows that the rules regulating the effect of security rights *inter partes* differ considerably throughout the European Union, notably the obligations that can be secured, the obligations on the parties during the existence of the security and the obligations that fall upon the creditor when it comes to enforcement. However, he recognises that there are some consistencies, for example, in relation to the recognition of both ‘genuine’ and ‘functional’ securities and the principles that the security provider must not prejudice the security right and the creditor must not adversely affect the security provider’s interest in the subject matter of the security. Steven concludes that such consistencies are a useful starting point if an attempt to harmonise the law is made, although harmonisation of the contractual effects of a security cannot be carried out in isolation from the relevant property law. Security obligations are of little value if the security is not effective from the point of view of property law.

In response, Vriesendorp (Tilburg) agrees with this last observation of Steven’s to the extent that the security right is a derivative from property law, such as is the case with mortgages, pledges and the like. From a Dutch law perspective, however, he disagrees with some of Steven’s other observations. Finally, he agrees with Steven’s concluding remark that much work lies ahead should we wish to harmonise, but he predicts a slightly different approach. According to Vriesendorp, harmonisation attempts in the area of security law should focus on the creation of a minimum level to protect the interests of both parties. They should not lead to rules that are too detailed and that could petrify future developments.

Dirix (Leuven) discusses the effect of security rights vis-à-vis third persons. In his essay different topics are addressed: first, the enforceability of security rights against third parties; second, the rules for determining the ranking between secured creditors; third, possible conflicts about priority; fourth, the question to what extent a secured creditor who enforces his security right owes a duty of care towards other creditors; and, finally, some problems arising in connection with the transfer of secured claims. Dirix shows us that there has been a development towards harmonisation during
the past decade as a result of legislative initiatives and case law. The new rules on the assignment and pledging of claims, the recognition of reservation of title and the implementation of the Financial Collateral Arrangements Directive are good examples of the harmonisation through legislative initiatives. The gradual limitation of the impact of statutory preferences is another development, according to Dirix. An example of harmonisation through case law is the acceptance of the purchase money priority by the French Cour de Cassation and the German Bundesgerichtshof. The requirement of publicity no longer seems to be considered as an essential condition for a security right's effectiveness vis-à-vis third parties and is replaced by other requirements. Nowadays hidden security rights are recognised in many jurisdictions. Dirix ends his contribution with the conviction that gradual evolution is perhaps the most realistic way to achieve harmonisation within Europe.

Lukas (Linz) comes to the conclusion that there is a definite need to eliminate the non-recognition of security rights between member states and the resulting impairment of fundamental freedoms. Private international law is an important instrument to solve this problem. However, in the interest of the internal market, there is also a growing need for uniform European standards with regard to collateral security law. According to Lukas such standards could help to bring credit costs in the member states more into line with each other and thus remove barriers to competition within the Community. In the creation of such standards, the responsible EU institutions would be able to orient their work on the extensive preparatory work already done by UNCITRAL and other institutions.

1.2.3 Recognition and Adaptation of Foreign Security Rights

Drobnig (Hamburg) discusses the recognition and adaptation of foreign security rights in the case law of the member states. In the EU study on the interaction of contract law and property law the following question was asked to businessmen and legal practitioners: 'have problems arisen in business transactions with foreign parties (in other member states of the EU) because of differences in the legal rules governing acquisition and loss of ownership of movable property?' As Drobnig points out, the summary of the replies to the question demonstrates 'a widely shared feeling of dissatisfaction on the issue of recognition of security rights in exported goods'. Drobnig investigates the question whether or not and to what degree this general feeling of dissatisfaction and insecurity about security rights in export goods in intra-European trade is justified in the old member states. He concludes that the survey of court practice in the member states on the recognition and non-recognition of security rights in goods imported from other member states as well as the reaction of stakeholders demonstrates the great differ-