'A Labyrinth of Creditors'

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2 A labyrinth of creditors: a short introduction to the history of security interests in goods

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1. Introduction

The history of security interests in movables on the European continent begins with the 'reception' of Roman law in the guise of Justinian's *Corpus Iuris Civilis* in the Middle Ages.[1] As with any code, Justinian's codification forms the conclusion of an era in the development of the law. Legal concepts not incorporated into the code, like the ancient *fiducia cum creditore*, were consequently concealed from the legal consciousness for ages, until some of them were drawn from the collective subconscious of the civil law in the course of the nineteenth century. An assessment of the Roman origins of the continental European system of security interests in movables is important, particularly since many aspects of the modern system have been consciously developed as a reaction to the Roman system. The current statutory provisions on the creation of a valid pledge, for example, are only comprehensible if it is appreciated that they were formulated as a response to the deviating provisions of Roman law. It will, therefore, be necessary to glimpse briefly the Roman system of security interests in movables as contained in Justinian's codification.

[1] On the reception of Roman law see especially Francesco Calasso, *Medio Aevo del Diritto* (1954), *passim*; Fr. Calasso, *Introduzione al Diritto Commune* (1970), *passim*; Helmut Coing, *Europäisches Privatrecht* I (*Älteres Gemeines Recht*) (1985) ff.; John Dawson, *The Oracles of the Law* (1968) 125 ff., 177 ff. and 263 ff.; Paul Koschaker, *Europa und das römische Recht* (1966), *passim*; and Fr. Wieacker, *Privatrechtsgeschichte der Neuzeit* (1967), *passim*.

2. Justinian Roman law

After the demise of the concept of *fiducia*,[2] Roman law recognised only two proprietary security interests, *pignus* and *hypotheca*. Both interests differed from *fiducia* in the sense that with *pignus* and *hypotheca* the absolute legal title to the object of these security interests remained with the chargor (pledge-debtor), whereas *fiducia* implied a transfer of title by the chargor to the chargee (pledge-creditor).[3] The two remaining proprietary security interests of Roman law were *iura in re aliena*, special proprietary interests in goods belonging to another, mostly (but not necessarily) the debtor. This fundamental fact has some important consequences, dominating the law on this subject to date. One is that the chargor remains entitled to dispose of his property as he sees fit, even though a security interest has been vested in it. He may charge his property again to secure another debt. Furthermore, he may even transfer his title to another person without the permission of the chargee. Any contract to the contrary only has effect as between chargor and chargee[4] and does not affect the rights of third parties, such as supervening chargees and new owners. The original chargee, however, has a security interest, which ranks higher than any security interest subsequently established and which vests in him the right to recover the object of his security interests from any new owner. It would, therefore, be quite wrong to construe the creation of a security interest as a means to separate the objects of security interests from the rest of the assets of the chargor. In spite of the creation of a security interest, they still constitute a part of the assets of the chargor, and are even subject to the rights of his other, non-secured creditors. All the chargee has is a right to satisfy his debt out of the sale of the objects of his security interest

[2] On *fiducia* see M. Kaser, *Das romische Privatrecht* (RP) I (1971) 144 f. and 460 ff.; RP II (1975) 275 and 313; and especially G. Noordraven, *De 'Fiducia' in het Romeinse recht* (1988).

[3] Unless otherwise indicated, I will use the term 'charge' throughout in the broad sense, as a 'real' burden attaching to a certain part of the debtor's property as a security interest for the payment of a debt. The words 'chargor' and 'chargee' stand for the grantor and the grantee of a proprietary security interest.

[4] There is one passage in Justinian's Digests (D. 20,5,7,2 (Marcianus)) containing a reference to a contract between chargor and chargee, restricting the chargor's powers of disposition. The passage has been the subject of controversy, as it seems superfluous in view of the fact that the chargee may successfully sue anyone in possession, including a new owner, for recovery. See e.g. Schlichting, *Die Verfugungsbeschrankung des Verpfanders im klassischen romischen Recht (1973)*; Wacke, *Rivista Internazionale di Diritto Romano e Antico* 24 (1973) 184 ff.; and Kaser, *Tijdschrift voor Rechtsgeschiedenis* 44 (1976) 283 ff.

with preference over other creditors. That right, however, is a right *in rem*. In order to enforce it, the chargee has an action for recovery of the objects of his security interest against anyone in possession, the *actio Serviana*. It should be stressed, however, that the nature of that action differs from that of the *rei vindicatio*, the proprietary Roman action of the owner for specific restitution of his property. The object of the *actio Serviana* is recovery of the objects of security interests by way of distress, whereas the *rei vindicatio* presupposes an immediate right to possession, irrespective of any particular purpose other than restitution of possession.

Hence there are frequent conflicts of interests between secured creditors on the one hand and the 'trustee in bankruptcy', the *curator bonorum*, on the other in many civil law systems. In Roman law, there was no specific duty of sale on the part of a secured creditor, as there is in modern civil law jurisdictions, but the chargee could be forced to surrender the objects of his security interest to the chargor whenever the latter wanted to dispose of his property.[5] One may, therefore, assume that the *curator bonorum* was able to block an action for recovery by the chargee whenever the latter was not willing to sell. The explanation is, of course, that the equity in the property granted as security that is the surplus value thereof remained with the chargor.

The legal dichotomy between movables and immovables is fundamental to many, if not all, modern continental European legal systems, especially in so far as security interests are concerned. This was not the case in Roman law. There was no rule restricting non-possessory security interests to real (immovable) property and possessory security interests to (movable) goods. On the contrary: pledge (*pignus*), a possessory security interest, could be vested in personal as well as real property, whereas 'hypothec' (*hypotheca*), the non-possessory security interest of Roman law, could also be vested in real, as well as personal, property. It was only as a matter of convenience that pledge (*pignus*) was associated with goods (movables), because they are more suitable for delivery than real property (land).[6] The two security interests of Roman law, accordingly, merely differed in so far as their respective modes of creation were concerned, a pledge being created by delivery of possession (*traditio*) and a *hypotheca* by way of a simple contract:

[5] D. 13,7,6 pr. (Pomponius) and see on this passage Noordraven, *Bullettino di Diritto Romano* 83 (1980) 247 ff.

[6] D. 50,16,238,2 (Gaius).

D.13,7,9,2 (Ulpianus): 'Pignus' is properly used when possession has been delivered to the creditor and 'hypotheca', even if possession is not transferred to the creditor.[7]

A Roman pledge (*pignus*) differed radically from a modern European 'pledge'. Some of the problems encountered in modern European law can only be understood if it is kept in mind that this difference can be traced to the origin and development of the Roman concept of *pignus*.

Pignus was created by *traditio*, which is by surrender of *civilis possessio* to the chargee. The latter did not become a mere bailee (detentor), as he is in modern continental European civil law, but a possessor, the pledgor not even retaining constructive possession. A subsequent surrender of possession by the pledgee to the pledgor, however, did not terminate his security interest, as is the case in modern continental European systems. Consequently, the object of a *possessory* security interest was not infrequently leased to the chargor:[8]

D. 13,7,35,1 (Florentinus): 'Pignus' merely confers possession on the creditor, because it remains the property of the debtor: the debtor, however, is allowed to use his own property at the will of the pledgee or as a lessee.[9]

D. 13,7,37 (Paulus): Whenever I have leased a pledge delivered to me to the owner, I retain possession by the lease, because before the debtor took the lease, it was not his possession, all the more so because I have the will to retain possession and a lessee cannot have the will to obtain possession.[10]

Whenever property had been charged by way of pledge and was subsequently bailed (transferred) to the chargor, there was practically no difference between *pignus* and *hypotheca*. This is the apparent reason for the observation by the Roman lawyer Marcianus that 'the difference between *pignus* and *hypotheca* is purely verbal'.[11] The phenomenon also helps to explain why Roman sources use the concept of *pignus* in a rather cavalier way: sometimes it stands for a special security interest, created

[7] 'Proprie pignus dicimus, quod ad creditorem transit, hypothecam, cum non transit nec possessio ad creditorem.'

[8] See Tondo, *Labeo* 5 (1959) 157 ff.; and Kaser, *Studia et Documenta Historiae et Iuris* 45 (1979) 1 ff.

[9] 'Pignus manente proprietate debitoris solam possessionem transfert ad creditorem: potest tamen et precario et pro conducto debitor re sua uti.'

[10] 'Si pignus mihi traditum locassem domino, per locationem retineo possessionem, quia antequam conduceret debitor, non fuerit eius possessio, cum et animus mihi retinendi sit et conducenti non sit animus possessionem apiscendi.'

[11] D. 20,1,5,1 (Marcianus): 'Inter pignus autem et hypothecam tantum nominis sonus differt.'

by surrender of possession, sometimes it is synonymous with the concept of 'security interest' in general. On reflection, therefore, the antithesis of *pignus* and *hypotheca* in Roman law does not necessarily correspond to the distinction between possessory and non-possessory security interests of modern civil law systems: a Roman 'pledge' might well have amounted to a non-possessory security interest. It might even have been created by constructive delivery (*constitutum possessorium*), so that the chargor never lost factual possession of the objects securing his debt to the chargee. The famous Roman lawyer Ulpian had already observed that creditors frequently left their debtors in actual possession of property charged by way of pledge (*pignus*).[12]

Roman law found itself in quite a predicament, due to the fact that it was possible in *all* types of security interests to leave the objects of security in the hands of the debtor. The total absence of any system of publicity created serious problems in practice, especially in so far as the ranking of subsequent chargees of the same property was concerned. Ranking has been dominated by a simple rule of thumb – *prior tempore, potior iure*[13] – for most of the history of Roman law. A refinement was introduced only relatively late. In AD 472 the emperor Leo decreed that a security interest, created by 'public instrument', or a written memorandum signed by three witnesses, ranked higher than preceding security interests not created in this way.[14] It should be stressed that the emperor did not invalidate security interests not created in conformity with this provision. On the contrary: even after 472 all security interests, created in accordance with the ancient rules of the Roman common law, were still valid, albeit that security interests created in accordance with Leo's provision had priority over all security interests not complying with his formalities. The significance of the emperor's innovation was that he introduced an additional rule of preference, thus confusing matters even more. After 472 third parties, having acquired title to goods charged by a former owner, continued to be confronted by chargees till then unknown to them with actions for recovery of the property for the execution of a predecessor's debts.

Another factor that considerably complicated the Roman system of security interests was that they could be vested not only in individual parts of the debtor's estate, but in his entire estate as such.[15] The former

[12] D. 43,26,6,4 (Ulpianus): 'cottidie enim precario rogantur creditores ab his, qui pignori dederunt'. See also D. 43,26,11 (Celsus).

[13] C. 8,17 (18),3. See also VI°, *De regulis iuris*, reg. 54.

[14] C. 8,17,11,1.

[15] D. 20,1,1 pr. (Papinianus).

were designated as 'special' security interests and the latter as 'general' security interests. There were no fundamental differences between 'general' and 'special' security interests, their relationship being determined by the same ancient rules of preference and by Leo's decree of 472. Consequently it frequently occurred that older general security interests had priority over later special security interests, even if the latter had been created by transfer of possession of the object of security to the chargee.[16]

I will confine this chapter to consensual security interests, namely those created by virtue of an agreement. It should be noted, however, that there were many 'special' as well as 'general' *statutory* security interests in Roman law. They must be distinguished from mere privileges, because the latter are only concerned with priority (preference), whereas the former were a genuine charge on the property of the debtor. Of course, some of these statutory security interests were indeed 'privileged', in that they had priority (preference) over older consensual security interests.

Even disregarding the confusing complexity of 'general' and 'special' pertaining to consensual as well as statutory security interests, the Roman system of security interests had one main deficiency: the absence of an adequate system of publicity, especially in so far as movables were concerned. Without publicity, Roman law could only maintain its system of security interests by calling in the assistance of criminal law by rendering it a crime to transfer property without disclosing to the transferee the charges with which the property was burdened (*stellionatus*).[17]

3. Later developments in the European *ius commune*

At the end of the fifteenth century, the Roman system of security interests had become part of the law of practically all European countries, with the exception of England and Wales. This system drew sharp criticism from the famous Dutch lawyer Johannes Voet (1647–1713), whose *Commentarius ad Pandectas* was regarded as an authoritative restatement of the European *ius commune* all over the European continent and in Scotland up to the nineteenth century. He characterised the system as 'a labyrinth of creditors, where lawyers creep around on winding and tortuous tracks'.[18] The deficiencies of the system were, however, not addressed

[16] D. 20,4,2 and 20,5,1 (Papinianus). [17] D. 47,20,3,1 (Ulpianus).
[18] *Commentarius ad Pandectas*, ed. Geneva 1757, Lib. 20, tit. 4, no 17.

by the introduction of an adequate system of publicity and registration, but by gradually eliminating some, if not all, of the consequences of the Roman non-possessory security interest of *hypotheca*, at least in so far as movables were concerned.

In order to avoid misconceptions, it should be emphasized that the phenomenon known as the 'reception' of Roman law on the European continent and in Scotland did not bring about a European 'common law'. Apart from regional and national differences in customary and statutory law, Roman law only had the status of a subsidiary and never as an exclusive source of law on any subject. Consequently, there were considerable variations in the extent to which the Roman system of security interests had been incorporated into the law of most European countries. This chapter has been written on the basis of 'Roman–Dutch' law, not because it still obtains in the Republic of South Africa, but because it was widely considered an outstanding example of the 'modern application' (*usus modernus*) of Roman law. This changed only after the fame of the Dutch authors of the seventeenth and eighteenth centuries was eclipsed by the celebrated German 'Pandectists' of the nineteenth century. By that time, however, the traditional system had practically ceased to exist everywhere else on the European continent.

In Holland, as in some other European countries, the relationship between 'general' and 'special' security interests was placed on a different footing to Roman law. 'Special' security interests were granted preference over 'general' security interests.[19] This was the first step in the development of the modern continental 'specificity principle' that only allows security interests in specific assets of the debtor and abolishes (at least in theory) the old Roman 'general' security interests. Another new development was that in some, but certainly not all, European 'civil law' jurisdictions all hypothecs, 'general' as well as 'special', were made subject to the ancient customary maxim *mobilia non habent sequelam*, 'meubles n'ont pas de suite' ('movables cannot be traced into the hands of third parties').[20] Whenever personal property subject to a hypothec

[19] The so-called 'Political Ordonance' of 1580 is to be found in *Groot Placaet Boek* I, 329.

[20] It has already been emphasised in the text that the 'reception' of Roman law did not provide the European continent and Scotland with uniformity of (private) law: the differences between the various regions and countries could be substantial. This applies especially to the question whether or not the rule *mobilia non habent sequelam* had been adopted in a particular region. In the Saxon territories of the German empire it did not apply to (special or general) non-possessory security interests. The only exception concerned a floating charge on the stock-in-trade of a shop: see Carpzov, *Jurisprudentia forensis Romano-Saxonicus*, Pars II, const. 23, definitio 12 and 13.

was transferred to a third party, that security interest expired.[21] Consequently, hypothecs on movables could only be enforced as long as the chargor was still in possession. The question now was whether this also applied to a non-possessory pledge where the pledgee was not in possession, either because the security interest had been created by constructive delivery (*constitutum possessorium*), or because the pledgee had restored actual possession to the pledgor as his bailee.

Voet held that all non-possessory security interests, be they a hypothec or a non-possessory pledge, were subject to the maxim *mobilia non habent sequelam*.[22] He went even further by suggesting that security interests in movables could only be validly created by transfer of possession to the creditor, thus virtually eliminating the Roman hypothec on movables.[23] His opinion was explicitly rejected by the 'High Council' of Holland, the highest court of judicature in Holland at the time, in an important decision of 13 November 1737.[24] The case concerned a shopkeeper, who had transferred her stock-in-trade to a creditor by way of constructive delivery, obviously in order to avoid the rules applying to hypothecs. The court felt obliged to determine the true nature of the transaction by considering the actual words used by the parties. It found that the parties actually intended to create a security interest by way of constructive delivery. What had actually happened, therefore, was that, despite Voet's contrary opinion, a valid pledge on the stock had been created by constructive delivery. The 'High Council' adhered to this precedent throughout its existence.[25] Consequently, shortly before the introduction of the first Dutch Civil Code (in 1809), the law of Holland recognised no less than four kinds of security interests in movables: possessory pledge (*pignus*, with the pledgee retaining possession), a hybrid 'non-possessory' kind of pledge, hypothec and, of course, the general hypothec on all the movable assets of the debtor.

[21] Grotius, *Inleidinge* II, 48, 29. See Pothier, *Traité de l'Hypothèque*, Ch. premier, sect. II, § 1 (*Oeuvres de Pothier* VII, Paris 1818, 315) on similar rules in Normandy and some other French territories.

[22] *Commentarius ad Pandectas* 20,1,12.

[23] *Ibid*: 'ipsi rei mobilis possessioni incumbere debere creditorem'. See also van der Linden, *Regtsgeleerd Practicaal en Koopmans Handboek* I,12,3.

[24] Van Bynkershoek, *Observationes tumultuariae* IV, no 3051.

[25] See Pauw, *Observationes tumultuariae novae* I, no 187 (23 Sep. 1746). It should be stressed that contemporary legal practitioners were largely unaware of the opinions of the court, because at that time judicial decisions were given without any reasoning. The reports of Bynkershoek and Pauw were not published until the twentieth century. This curious phenomenon helps to explain why the opinion of Voet remained influential, despite the fact that, as we now know, it was explicitly rejected by the 'High Council'

The situation in Scotland was (and is) less complicated. The Roman hypothec on movables has never been incorporated into Scottish law.[26] Due to the close relationship between Roman-Dutch law and Scottish law,[27] the authority of Voet was sufficient to secure the rejection of pledges created by way of constructive delivery (*constitutum possessorium*) and the introduction of the rule that a pledge is destroyed whenever possession is restored to the pledgor.[28] It hardly needs emphasis that the law of Holland, or that of any other country with similar legal rules, did not accept the concept of a fiduciary transfer of title to movables by way of constructive delivery for the purpose of creating what is essentially a security interest in the movables thus transferred.

The opinion of Voet that transfer of possession was necessary for the creation of a charge prevailed in Scotland and in the 'Roman-Dutch' law of the Republic of South Africa. Attempts to by-pass this strict rule included fiduciary transfer by way of constructive delivery and a sale and lease-back transaction. Both mechanisms failed in Scotland, whenever possession was not transferred *de facto*, i.e. whenever transfer of title was effected by way of a *traditio ficta*. Similar attempts have also been frustrated in South Africa.[29] New possibilities occurred in Scotland after the introduction of the Sale of Goods Act in 1893. In contracts of sale of goods, the Act abolished the ancient Roman rule that title in the goods can only be transferred by *traditio* and introduced the common law rule that title passes on conclusion of the contract of sale.[30] The new system of transfer of title seemed to open an opportunity to create security interests in movables without transfer of possession to the chargee by way of sale and lease-back transactions. These attempts have also failed.[31]

[26] Dalrymple of Stair, *Institutions of the Law of Scotland*, ed. Walker IV,25,1 and Bell, *Commentaries on the Law of Scotland* II 25: 'in this country, conventional hypothecs on movables have no force even against personal creditors'. For similar rules in the 'Coûtumes de Paris' and those of Orléans see Pothier, *Traité de l'Hypothèque*, Ch. premier, sect. II, § 1 (*Oeuvres de Pothier* VII, 315).

[27] See *Stewart v LMS* (1943) Ses. Cas. (House of Lords) 19, at pp. 38–39 per Lord MacMillan.

[28] See *North Western Bank v Poynter* (1894) 21 Rettie 513, at 525 and Bell's *Commentaries on the Law of Scotland* II 22. The decision of the Court of Session was reversed on appeal by the House of Lords (*North Western Bank v Poynter* [1895] AC 56), bringing the law of Scotland in line with the common law of England, which adheres less strictly to the dispossession of the pledgor (see *Reeves v Capper* (1838) Bing (NC) 136; 132 ER 1057).

[29] See *Vasco Dry Cleaners v Twycross* (1979) 1 SA 603 A and van der Merwe, *Sakereg* 688 ff.

[30] C. 2,3,20 and Lord Blackburn's dicta in *M'Bain v Wallace & Co.* (1881) 8 Rettie 106 (House of Lords) 111 f.

[31] See the cases cited in Walker, *Principles of Scottish Private Law* II 1582 (7).

4. Security interests in movables in the continental European codes

The French *Code civil* (1804) concluded the process of the demise of the Roman hypothec on movables in France by requiring transfer of possession for the creation of a security interest in movables ('nantissement')[32] and by limiting hypothec to real property (immovables).[33] The creation of pledge ('gage'), by way of constructive delivery, as well as the possibility of allowing the pledgor to hold the movable property on behalf of the pledgee (bailment), were effectively eliminated by article 2076 Cc: 'Dans tous les cas, le privilège ne subsiste sur le gage qu'autant que ce gage *a été mis et est resté* en la possession du créancier, ou d'un tiers convenu entre les parties' (italics added). The old Dutch Civil Code (1838),[34] the old Italian Civil Code (1865),[35] the Spanish Civil Code[36] and even the German Civil Code of 1900[37]contained similar provisions. The German Bankruptcy Act ('Reichskonkursordnung') of 1877 already provided[38] that security interests in movables that had not been created by a permanent transfer of possession to the chargee created no preference, thus finally abolishing the ancient Roman hypothec in movables ('Mobiliarhypothek') in Germany as well.[39] I will leave an analysis of the way in which modern continental European law has been able to cope with these provisions to others and confine myself to general observations on security interests in movables on the European continent during the nineteenth century.

From a modern perspective, it seems strange that the abolition of non-possessory security interests in movables in continental European codes did not meet with stronger resistance from banks and at least a considerable portion of the business community. The statutory provisions forced

[32] Articles 2017–2072 Cc. It is usually emphasised in French textbooks (see e.g. Ripert and Boulanger, *Traité de Droit civil* III, Paris 1958, no 52 (19)) that the concepts of 'nantissement' and 'gage' originate from ancient French customary law, rather than from Roman law. True as this may be, one cursory look in Pothier's *Traité du Contrat de Nantissement* suffices to conclude that they were construed and applied on the basis of the Roman concept of *pignus*. A 'nantissement' without 'tradition réelle' by the pledgor to the pledgee was even construed as a Roman *hypotheca*: see Pothier, *Traité de l'Hypothèque*, Ch. IV, article 1, § 1.

[33] Article 2118 Cc. Later statutory provisions have extended 'hypothec' to aeroplanes and ships above a certain tonnage.

[34] Article 1198 O(ud) BW (1838), repealed in 1992.

[35] Article 1882 *Codice civile del Regno d'Italia* (1865).

[36] Article 1863 *Código civil.*

[37] §§ 1204, 1205 and 1253 BGB.

[38] RKO § 14.

[39] On this development see Hromadka, *Die Entwicklung des Faustpfandprinzips im 18. und 19. Jahrhundert.*

the pledge-debtor to part with possession of his movable assets, thus rendering them unproductive, a consequence that may not even have been in the interest of his creditor. The pledge-creditor, on the other hand, was forced to store and maintain goods at a high cost without even being allowed to use the goods himself. In my submission this extraordinarily impractical and ill-considered statutory arrangement can be explained by the following observations.

First, the banking world of the late eighteenth and early nineteenth centuries was, in my opinion, not structured to provide business capital to the industrial community on the basis of security interests in the stock-in-trade and machinery of its clients. Although the banks did indeed finance *trade* on a large scale, this was more often than not done on the basis of personal security (guarantees), rather than on the basis of security of a proprietary nature. An entrepreneur in need of credit to expand his industrial activities was usually dependent on sources other than banks. Hence the proliferation of limited partnerships in the nineteenth century. Presumably banks only explored forms of security other than guarantees after the advent of modern business corporations. This structural change in the financing of industrial activities by banks may well have originated in the oversupply of money on the German market as a result of the reparations made by France after the war of 1870–1871. Was this the economic origin of the German 'Sicherheitsübereignung'?

Secondly, the business community was not severely hampered by the provisions of the new codes. Long before their introduction, the standard procedure in Amsterdam and other important ports was to transfer property stored in warehouses by transfer of the warrants (bills of lading)[40] and to charge such goods by pledging the warrants to a creditor.[41] These practices were even sanctioned in certain codes, for example in the Dutch Code of 1838.[42] It is not surprising that this commercial practice inspired the first French mechanisms to introduce non-possessory security interests in movables after the introduction of the *Code civil*.

[40] See the eighteenth-century cases reported in Pauw, *Observationes tumultuariae novae* I, nos 490, 556 and II, no 627.

[41] *Ibid.*, III, no 1490 (a case from 1779).

[42] Article 670 of the Dutch Civil Code of 1838; the provision was repealed in 1934. Of particular interest is van der Lelij, *Levering van roerende zaken door middel van een zakenrechtelijk waardepapier* 3–15.

5. Common law and civil law

English common law also recognises two security interests in goods, one being possessory, namely pledge or pawn, the other being non-possessory, namely the chattel mortgage. The suggestion has even been made that these two common law security interests corresponded to the Roman security interests: pledge being essentially the Roman *pignus*, the nature of the (chattel) mortgage being basically the same as that of the Roman *hypotheca*. This equation, however, was explicitly rejected in the famous case of *Ryall v Rolle* (1749).[43] Burnet J observed correctly that, according to Roman law, delivery of possession was only required for the establishment of a security interest in the case of pledges, as it was – and is – according to common law. However, the learned judge expressly and unequivocally rejected the suggestion that the common law (chattel) mortgage can be identified with the Roman hypothec.

> An hypotheca gave only a lien and no property with a right to be satisfied on failure of the condition and a mortgage with us is an immediate conveyance with a power to redeem and gives a legal property.

It is quite remarkable that Burnet J tried to define a common law mortgage by reference to a text in the *Corpus Iuris*, to wit C.4,54,2:

> If your parents have sold land on condition that it be restored if either they themselves or their heirs have at some time or within a certain period offered to repay the price and the heir of the purchaser is not inclined to keep his part of that agreement, whereas you are prepared to satisfy him, a (personal) action on the basis of that agreement will be given to you.[44]

The Judge remarked that this was the description of an English mortgage in Roman law and also referred to C.4,54,7.[45] These observations provide us with an excellent description of the common law mortgage

[43] 1 Atk. 165; 1 Wils. 260; 1 Ves.Sen. 348; 9 Bli.N. S. 377; 26 ER 107; [1558–1774] All ER 82.

[44] 'Si fundum parentes tui ea lege vendiderunt, ut, sive ipsi sive heredes eorum emptori pretium quandoque vel intra certa tempora obtulissent, restitueretur, teque parato satisfacere condicioni dictae heres emptoris non paret, ut contractus fides servetur, actio praescriptis verbis vel ex vendito tibi dabitur.'

[45] 'If the person you have mentioned has bought from you on condition that the thing sold ought to be restituted if a certain amount has been paid within a certain period, you cannot bring an action under our "rescript" that the agreement be annulled. But if he tries to back out of his obligation by retaining that thing on account of his ownership, you can secure your interest by the remedies of signification, deposition and sequestration (i.e. of the money to be paid).' ('Si a te comparavit is cuius meministi et convenit, ut, si intra certum tempus soluta fuerit data quantitas, sit res inempta, remitti hanc conventionem rescripto nostro non iure petis. Sed si se

in terms of Roman law. The texts used by Burnet J have been taken from section 54 of the fourth book of Justinian's Code, inscribed *De pactis inter emptorem et venditorem compositis* ('On the conditions agreed upon between buyer and seller'). The common law mortgage is thus construed as a conditional sale, vesting the general proprietary interest in land or chattels thus mortgaged in the mortgagee. These provisions from Justinian's Code played a crucial role in the development of a new kind of non-possessory security interest in movables in Europe during the nineteenth century.

Most continental European codes, like the French *Code civil*,[46] the Dutch Civil Code of 1838,[47] and even the German Code of 1900,[48] contain provisions derived from this passage in Justinian's Code. These provisions, known as 'faculté de rachat' or 'vente à réméré' in France, concern the stipulation by a seller to redeem his property on tender of the price. Roman law also provided for this kind of contract, not, of course, as an alternative to security interests for which there was no need, but to regulate an option granted to a seller to redeem his property. One possibility was that his option merely conferred a right *in personam*, not a right *in re*. After the introduction of the strict rules on the creation of a pledge in the European codes and the elimination of the Roman hypothec on chattels, these statutory provisions on the right of redemption were relied upon to by-pass the strict statutory provisions on the creation of security interests in movables. Such attempts met with varying degrees of success in Europe, thus causing a genuine divide between the European legal systems. In most jurisdictions, for example in France, these attempts have totally failed. The courts looked beyond the form of these transactions and often found that an apparently valid form concealed an essentially illegal substance.[49] Germany and the Netherlands, however, followed a substantially different approach.

First the German Bankruptcy Act practically abolished the old hypothec on movables by restricting preference (priority) over the general

subtrahat, ut iure dominii eandem rem retineat, denuntiationis et obsignationis depositionisque remedio contra fraudem potes iure tuo consulere.')

[46] Articles 1659 ff. Cc.

[47] Articles 1555 ff. Dutch Civil Code of 1838; the provisions were repealed in 1992.

[48] §§ 497 ff. BGB.

[49] See, for example, the important decision in *Loewenstein, Polak & Co. C. Decaux*, Req. 11 Mar. 1879, D. 79.1.401. The *Cour de cassation* ruled (Req. 21 Mar. 1938, D.H. 1938.2.57) that the decision whether a particular contract is a valid 'vente à réméré' or an illegal security interest is a matter to be decided on the merits of the circumstances of each individual case by the courts taking notice of the facts.

creditors in bankruptcy to pledges created by transfer of possession to the pledgee. Only three years later, the new German *Reichsgericht* was confronted with two cases concerning an attempt to create a security interest in movables by means of sale and lease-back transactions. In one decision, the third civil division of the court decided that this transaction created a security interest in substance under the guise of a contract for the sale of goods with powers of redemption of the seller. It ruled that the contract was void.[50] In the other decision, however, the first civil division of the court held that such a contract was acceptable if it had been the genuine intention of the seller to transfer the true title to his creditor with a stipulation for redemption. The court regarded the fact that the economic purpose of the contract was to create a security interest as immaterial.[51] As long as the form and appearance of a genuine sale and lease-back was retained, a security interest could be created on the basis of a contract of sale and lease-back. The sale was naturally executed by constructive delivery, leaving the seller in possession and converting his powers of redemption into a legal or economic duty to redeem. Ten years later, the 'Reichsgericht' explicitly recognised that the *causa* for the constructive transfer of movable property could be the creation of a security interest in that property.[52] Thus, after a considerable lapse of time, *fiducia* was finally reintroduced in a civil law system. The Dutch 'High Council' followed suit in 1929.[53]

About the same time as continental European lawyers were in the process of reinventing the ancient Roman *fiducia cum creditore* by transforming Justinian's provisions on conveyance of property with a stipulation for redemption to supersede the strict Roman provisions on conveyance, the character of a chattel mortgage – essentially a conveyance

[50] RG 24 Sep 1880, RGZ 2, 173 As the case had to be decided according to Roman law, the court based its decision on D 18,1,80,3 (*Labeo*) and C 4,22,3

[51] RG 9 Oct 1880, RGZ 2, 168 (170) 'Es ist nicht nur rechtlich zulassig, sondern auch in haufiger Ubung, daß einem Glaubiger zu seiner Sicherstellung wegen einer personlicher Forderung von seinem Schuldner ein Vermogens-Objekt in der durchaus ernstlichen Absicht verkauft und ubertragen wird, daß der Glaubiger als Kaufer wirklicher Eigentumer und zur Ausubung aller Rechte eines Eigentumers befugt werden soll, der wirtschaftliche Zweck einer bloßen Sicherstellung aber dadurch erreicht wird, daß der Glaubiger sich durch Nebenabreden personlich verbindlich macht, unter gewissen vereinbarten Bedingungen das Eigentum dem bisherigen Schuldner zuruckzuubertragen' It is a curious but totally accidental coincidence that the formulation of this decision practically matches the important recent decision of the Dutch 'High Council', *In re Sogelease* (19 May 1995 (NJ 1996, 119)), almost verbatim

[52] RG 2 June 1890, RGZ 26, 180 [53] *Hoge Raad* 25 Jan 1929 (NJ 1929, 616)

of property with a stipulation for redemption[54] – was fundamentally changed in England. The legislative act which triggered this change was the introduction of Bills of Sale Acts (since 1878) and the requirement of registration. After then, 'chattel mortgages' were only allowed if the grantor had actually transferred possession to the grantee. Only then did the mortgagee enjoy preference over the general creditors upon his debtor's bankruptcy. Creditors have naturally tried to by-pass these provisions by returning to the archetype of non-possessory security in chattels of the common law, the conditional sale (the sale and lease-back or a hire-purchase contract). Insufficient attention has been paid on the continent, especially in the Netherlands, to the way in which English courts enforce the Sale of Goods Act. 'The court is to look through and behind the documents, and to get at the reality.'[55] More often than not, the court finds a sham or simulated security transaction behind an apparently valid transaction and refuses to allow a creditor to avail himself of a proprietary security interest created in this way.[56]

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[54] There is, however, a fundamental difference between a mortgage and a civil law transfer of title with a power (or duty) to redeem. English equity has transformed the common law right to redeem, a right *in personam*, into a proprietary interest *sui generis*, the 'equity of redemption'.

[55] *Maddel v Thomas & Co.* [1891] QB 230, at 234 per Lord Esher.

[56] See *Polsky v S & A Services* [1951] 1 All ER 185.

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