

Illustration: Grant Robertson

As safe as houses

This month Daniel Priestley, Counsel and Christopher Russell, senior counsel and Head of Litigation at Ogier take a look at the nature of a mortgage as security.

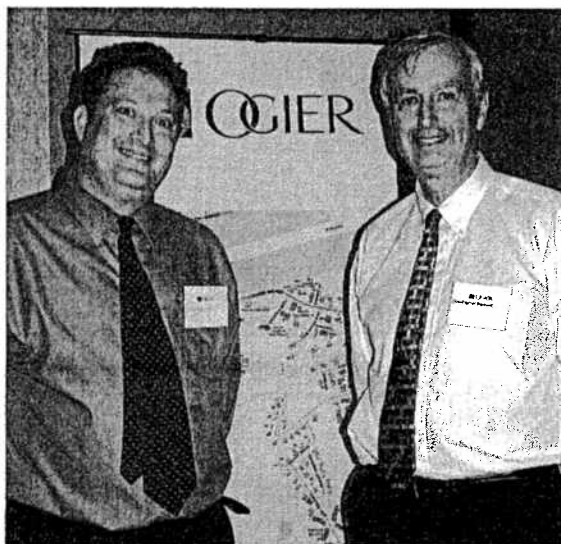
The nature of a mortgage as a form of security is of fundamental importance and, in legal terms, it is the giving of that security which enables the banks and other lending institutions to make the loans necessary to keep the wheels of the residential property market well oiled and therefore why, for the average person, a mortgage is a fact of life.

A security interest is a right given to one party in the asset of another party to secure payment or performance by that other party or by a third party. A security interest will generally possess the following characteristics:

- It is a right given by a debtor to a creditor in an asset;
- The right is by way of grant of an interest in the debtor's asset, not by way of reservation of title to the creditor;
- The right is given for the purpose of securing an obligation;
- The asset is given in security only, not by way of outright transfer;
- The agreement restricts the debtor's right to dispose of the asset free from the security interest.

In order to create a security interest, that security interest must be "perfected", which is the task we, as attorneys-at-law, perform on behalf of lenders in connection with the typical mortgage transaction. Our principal tasks are to investigate the borrower's title to the asset to be secured, and, upon verifying that there is good title, to ensure that the security interest "attaches" to the asset being used as security, which, in this case, is land.

The process of investigation of title is a vast subject in-and-of-itself and is therefore outside the scope of this discussion. Suffice to say, that the practitioner must approach the investigation of title in the same way he would do so if he were acting on behalf of a purchaser of the land. If the lender is forced to realise the security to pay off the loan, the lender would be in the same position as an owner of the property trying to sell it. The practitioner should seek to flush out any peculiarities relating to title to the property and, indeed, practical matters affecting the property so as to put his client in the best possible position to sell the property.



Daniel Priestley and Chris Russell

Potentially adverse matters to the lender's proposed interest in the property should be brought to the lender's attention at the earliest possible opportunity to enable the lender to re-evaluate whether or not it wishes to proceed with the loan. This re-evaluation is possible because any properly drawn facility letter agreement will make the advance of the loan subject to receipt by the lender of a satisfactory title report from the attorney acting.

Usually, the investigation of title will culminate in the giving of an opinion or report on title by the attorney to the lender. Very briefly, the statements in the opinion the lender should be looking out for are:

- that the borrower's title to the property is absolute and there are no encumbrances registered against the property which are potentially adverse to the lender's proposed interest in the property, except any such which will be released at completion;
- That the planning search carried out does not reveal any adverse matters, such as enforcement action;
- That replies to enquiries do not reveal any matters adverse to the lender's proposed interest in the property;

- That there are no unusual qualifications to the opinion;
- That, so long as the necessary procedures are followed to secure the loan over the property, the security document will be enforceable; and
- That the attorneys confirm that the

borrower has "good and marketable title" to the property.

The opinion will not provide any input on the financial aspects of the transaction and, in particular, whether or not the proceeds of sale of the property would be adequate to meet the borrower's obligations to the lender. This issue is entirely a matter for the lender to ascertain, which it will usually do by obtaining a valuation and applying a risk tolerance formula, which will take in factors such as loan-to-value and the borrower's income and any other assets the borrower may have to support his obligations, the precise terms of which vary from lender to lender.

The practitioner must then see to the securing or "attachment" of the security interest. The following elements must exist in order for the attachment to succeed:

- There must be an agreement for security;
- The asset to be given as security must be identifiable;
- The debtor must have an interest in the asset or power to give it in security;
- There must be some current obligation of debtor to creditor which the asset is designed to secure; and
- Any contractual conditions for attachment must have been fulfilled.

Registration is a relatively late addition to the laws relating to the perfection of security but, of course, registration is of fundamental importance in so doing. Next month, we will look at and explain the documents comprising a mortgage.

controls and procedures are in place relative to the scale of the business. That said, there is considerable personal liability in acting as a director to a hedge fund and therefore an individual director concerned with their personal reputation is best placed to determine the appropriate number of directorships to accept.

Determining factors in the number of hedge fund directorships an individual should accept will include the nature of the investment risk of each fund, the degree of leverage, short selling, quality of the third party administrator and auditor and how much reliance might be placed on them, whether the investment manager is regulated or not, past track record of the investment manager, whether the fund is single manager, fund of funds or has numerous portfolios under a SPC structure and many more factors. With so many factors, you can appreciate there cannot be some magic formula dreamt up by the regulator that determines the appropriate number of directorships.

There appears to be a lot of issues to assess before accepting a directorship. However, you have not mentioned the tax consequences for a fund yet this appears to be a hot topic in the UK media at present?

You are right, but this is less an issue about whether to initially accept a directorship on a fund and more an ongoing issue for the director to ensure it maintains the fund's "safe harbour" from taxation. Factors such as the location of board meetings and the composition of the board can affect a fund's susceptibility to tax or tax residence. It is preferable for the board to meet quarterly and to include face-to-face meetings but, as you might expect, this is not always possible. Where a director participates by telephone, this should be avoided if the director calling in from a taxable jurisdiction (such as UK, Ireland, HK etc.) is required to make the meeting quorate. It therefore