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978-1-107-18709-2 — Transfer of Immovables in European Private Law
Edited by Luz M. Martínez Velencoso , Saki Bailey , Andrea Pradi
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1 The Land Register in European Law: A Comparative and Economic Analysis

LUZ M. MARTÍNEZ VELENCOSO

1 The Land Register in European Law

1.1 The Land Register as a Way of Publishing the Transfer

In different European legal systems there are several models of Land Register. One of the functions of the legal system is to regulate the institutions by which rights are exchanged so that these transactions are secure and foreseeable. One of these institutions is the Land Register, which collects information on the ownership, content, reliability and expected revenue associated with rights over immovable property.[1] The Land Register therefore operates over a fundamental element of the economic system, the delimitation, attribution and protection of property rights.

By offering information on property rights, the Land Register reduces the costs associated with exchanges and facilitates the circulation of goods, and it can therefore be described as an instrument in the creation of wealth. This view is endorsed in a report published by the World Bank, the *World Development Report*.[2]

This contribution has been prepared within the Framework of the Research Project DER2013-42526-R, 'New Challenges of the Digital Society: Ownership, Contracts and Electronic Registers', funded by the Spanish Ministry of Science and Innovation.

[1] *See* Fernando Pomar Gomez, p. 1067, cited in Luz M. Martínez Velencoso, 'Transfer of Immovables and Systems of Publicity in the Western World: An Economical Approach', *Journal of Civil Law*, 6 (Summer 2013); P. Fernando Méndez González, 'La función económica de los sistemas registrales', 671 *RCDI*, 857, 881 (2002).

[2] World Bank, *World Development Report* (World Bank: Washington, DC, 2005), pp. 79–84. *See also* World Bank, *Plan to Market* (Oxford University Press, 1996), p. 89: 'For pledging to work, lenders need a cheap and easy way to determine whether a prior security interest exists against the property. Some advanced legal systems do this by maintaining a publicly accessible registry.'

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This same argument was put forward many years earlier, in the explanatory preamble to the Spanish Mortgage Act of 1861:

> Our laws on Mortgages stand condemned both by science and by reason as they neither guarantee property sufficiently nor exercise a healthy influence on public property. Furthermore, they do not establish firm bases for credit secured by real estate, they do not encourage the circulation of wealth, they do not moderate interest on money, they do not facilitate the acquisition of immovable property and they do not provide sufficient assurance to those who lend money on the basis of this guarantee. Given this situation the need for reform is pressing and indispensable for the creation of mortgage banks, to create certainty regarding ownership and other property rights, to combat the effects of bad faith and to free proprietors from the yoke of merciless usurers.[3]

The Land Register publishes information on the chain of transmission of a particular property and reduces the risk of transfers being carried out without the compliance of the title-holder. It also offers security to potential acquirers of a property by providing them with information concerning the temporal validity and the legitimacy of the transmitter's title to property.

To sum up, the Land Register lowers the risk that the buyer will obtain an invalid title without increasing the threat to the seller that he may lose his title to the property without his consent.

As we shall see a little later in this chapter, there are several different types of Land Registers (i.e. register of deeds, title register ...). Some of them attest to the ownership of a property whilst others offer mechanisms to protect property rights while leaving the question of establishing ownership to the rules governing possession. In some legal systems, the Land Register is the exclusive source of information about the title-holders of immovable goods, while in others it functions alongside a system of publicity based on possession.

From the perspective of an economic analysis, the publicity afforded by the Land Registry is of greater functional value than the publicity given by the mere possession of goods when these goods are costly. For other types of goods, the maintenance costs of this system of publicity exceed the benefits obtained from the reduction of the types of risk we have mentioned. Property registers are also understood to be more efficient when: the registered properties are not subject to frequent transmissions; the properties in question have a long economic life;

[3] Spanish Mortgage Act (8 February 1861), published in *Leyes hipotecarias y registrales de Espagña: Fuentes y evolución. I. Leyes de 1861 y 1869* (1974), pp. 223–395.

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and when the registered properties are susceptible to economic exploitation by several subjects at the same time (for example, when it may be possible to constitute limited real rights over the properties – such as a mortgage).

A property register can also be understood to be efficient when the descriptions of the registered property it provides, give more information about it than mere possession could.

1.2 The Rules for the Transfer of Property as an Instrument for Sharing Risk between the Transmitter and the Acquirer of a Property

There are currently several different types of systems in use for the transmission of immovable goods in Europe that have developed as a result of the different legal traditions throughout the continent.

The rules that govern the transmission of property are important as they provide an answer to a series of fundamental questions that arise from the circulation of property rights. Five of the most important of these questions are: (a) Who has the effective power of disposition over the property sold? (b) Who is responsible for any damages caused to third parties by the property? (c) Does the property constitute a guarantee for the creditors of the transmitter or the acquirer of the property? (d) Who supports the risk in case the property is damaged or perishes? (e) Who has the right to obtain the benefits produced by the property sold?

Broadly speaking, the main systems of ownership transmission in Europe can be divided into the following four categories:

(A) Legal systems such as the French legal system and those which developed under its influence (e.g. the Italian, the Portuguese and the Belgian legal systems), which recognise the transmission of ownership by contract, an agreement between the parties, which produces the effective transmission of property.

(B) Legal systems such as the German legal system and those over which it has exerted an influence (for example the Austrian, the Swiss and the Greek legal systems), in which the conclusion of a contract must be accompanied by a contract on the actual transfer of the property and the inscription of the transmission in the Land Registry. In most of these systems, the contract on the actual transfer of the property has been substituted by the inscription.

A characteristic of German law is that the contract on the actual transfer of ownership is disconnected causally from the contract that details the obligations of the parties, in such a way that a nullification

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or modification of the contract detailing the contractual obligations has no effect over the contract on the actual transfer and thus no effect on the validity of the transmission of property.

(C) The Spanish legal system shares some of the characteristics of both legal systems previously discussed. The Spanish system requires the conclusion of a contract (a title) and the *traditio* (the delivery of possession with the intention of passing ownership, which is the *modo* or correct form). These requirements are an example of how some aspects of the Spanish legal tradition have asserted themselves over the strong influence of the French tradition.

A distinctive characteristic of the Spanish system is the causal relation between the contract and the transmission of property. If the contract is invalid then the transmission of ownership cannot be said to have taken place.

(D) The common law system uses a complicated process known as 'conveyance' to transfer property. This process consists of various stages, and in some countries (such as the United Kingdom) the consummation of the process of acquisition is only achieved with the inscription of the title in the Land Registry.

From the perspective of an economic analysis,[4] an optimal system of property transfer would be one in which a single subject could be said to have: (1) an interest in safeguarding and conserving the physical condition of the property; (2) the legal means to protect the property; (3) physical contact with the property, so that a title holder would be in a position to see whichever steps might be necessary to take in order to safeguard and conserve the property. However, it is not within the power of the legislator to condition the transmission of the property and the actions associated with the transfer in such a way as to ensure that these three conditions always coincide. The legislator is forced to choose between conflicting interests and to distribute risk between the parties in one way or another.

The three conditions stated are not met in the solution provided by the French legal system. Sacco describes the French solution as 'pseudo consensual'[5] and attributes it to an intense dislike on the part of its

[4] *See* Roberto Sacco, *Conclusión: Congresso Internazionale Pisa–Viareggio–Lucca, 17–12 aprile 1990*, in Letizia Vacca (ed.), *Vendita e Trasferimento della proprietà nella prospettiva storico-comparatistica atti del congresso internazionale Pisa–Viareggio–Lucca*, 1, 17–21 April 1990 (Milan: Giuffrè, 1991).

[5] Sacco, *Conclusíon*, p. 900.

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creators of the obligation to give.[6] This obligation is substituted by the automatic effect of the transmission of the property. The obligation to give is characterised by the fact that the creditor, who has an effective interest in the condition of the property, does not have any legal action at his disposal to protect it. The authority to do so is held by the proprietor, who has a number of legal actions available to him to protect the property (such as the action to recover the property from the possession of third parties and the *actio negativa*).

As a consequence, the French legislator considered it advantageous to convert the buyer automatically into the owner rather than the creditor of an obligation to give. However, this consensual system has a weakness. While it transfers authority to protect the property in the hands of the buyer, who is naturally the subject interested in preserving the property in good condition, it means that the ability to protect the property is conceded to a subject that does not have it at his disposal. This subject, who does not have the possession of the property in question, is therefore not in a position to detect potential threats to it.[7]

A part of German legal doctrine has criticised the German model of property transfer. These authors feel that in the sale of immovable property, ownership should be transmitted on the payment of the price stipulated and the handover of the property.[8] This is the thesis held by members of the school of Carl Schmitt, who do not favour the

[6] Sacco, *Conclusíon*, p. 901.

[7] Spanish legal doctrine has come to the same conclusion; see, for example, Mariano Pérez Alonso, *El riesgo en el contrato de compraventa* (Madrid: Montecorvo, 1972), p. 254. This author considers the rule *res perit domino* to be a deviation from the original *periculum est emptoris* applied in Roman law and claims it was a creation of the natural law school of rationalists. This school of thought maintained that it was against the laws of nature and therefore wrong for the buyer to have to assume all the risk of a transaction, as it had traditionally been believed was the case in Roman law, and that in fact Roman law had not actually imposed this burden on the buyer. Hugo Grotius drew attention to several passages from the Roman period that he felt clearly showed that ownership was able to be transmitted, even without the act of placing the property in the possession of the buyer (the *traditio*), by the mere consent of the parties. However, even the consecration of the maxim *res perit domino* does not eliminate the injustice of the rule *periculum est emptoris*, because making the buyer the owner of a property without handing over to him the possession and the use of it is effectively the same as making him a creditor of the right to the property. In both cases the contractual risks are assigned to the detriment of the subject who has to pay the price.

[8] This is the opinion of Hans Brandt, 'Eigentumserwerb und Austauschgeschäft, der abstrakte dingliche Vertrag und das System des deutschen Umsatzrechts im Licht der Rechtswirklicheit', 120 *Leipziger Rechtswissenschaftliche Studien*, 322 (1940), which has been criticised by Heinrich Lange, 'Rechtswirklichkeit und Abstraktion', 148 *AcP*, 188 (1943).

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current model of property transfer in the German Civil Code (*Bürgerliches Gesetzbuch*, BGB). They dispute the necessity to distinguish between obligational contracts and contracts on the actual transfer of property.

The critics of this model draw on a wide range of historical sources to support their critique, including Roman law, ancient Germanic law, natural law philosophy and nineteenth-century Prussian law.

Another controversial issue in the German system of property transfer is the principle of abstraction. This principle states that contracts on the transfer of property are independent from their cause, which means that they produce effects even if the accompanying obligational contract proves to be invalid. The decision to incorporate the principle of abstraction in the legal system is a political decision taken by the legislator in an attempt to balance the conflict of interests generated between the transmitter of the property, the acquirer and his creditors, the successors of both parties and the interests of commerce.[9]

The principle of causality and the principle of abstraction are techniques used to distribute risk between the parties to a contract. The principle of causality better protects the interests of the creditors of both parties, because only the patrimony of their debtor is placed at their disposition and it does not protect the good faith of the acquirer's creditor based on the appearance of the situation created. In this way, a subject that has goods at his disposal is able to retrieve them from the patrimony of a third party, without his interests being secondary to those of the acquirer's creditors.

The principle of abstraction guarantees equality between the parties, because both the subject that transmits the property and the subject that acquires it only have legal actions based on their contractual obligations. According to the principle of causality this would not be the case, as it presents a danger that the seller might stake a claim to the property by means of the revindicatory action (*reivindicativo*) (which is used to defend a property right), while the purchaser of the property would only have legal actions based on the other party's contractual obligations.

In the opinion of Lange, the best property transfer system would be that which combined the principle of causality with a system of acquisition of property *a non domino*.[10] This would afford the parties protection

[9] This principle was included in the BGB due to the influence of Savigny. The celebrated German jurist considered just cause to be the agreement that the parties reach over the transmission of property whilst the property agreement itself (*Einigung*) is a separate legal act that does not depend on a contract outlining the obligations of the parties.

[10] Lange, 'Rechtswirklichkeit', n. 8, p. 188.

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against any possible defects in the underlying legal agreement and would also protect the interests of secure transactions and more generally of commerce.[11] This is the solution that Spanish legislators have opted for. While the Spanish system of property transfer is causal it also protects those that acquired their right from a subject that appeared in the Land Register as the title-holder of the property by maintaining the validity of their acquisition, even when the transmitter was not really the legitimate owner. It also protects the acquirer from any other resolution or revocation of rights that did not figure in the Land Registry at the time of transfer (art. 34 Spanish Mortgage Act).

2 The Economic Functions of the Land Register: A Comparative Analysis of the Different Land Registration Systems

2.1 Systems of Land Register in Europe

The legal systems of Europe differ not only in the rules they employ to regulate property transfer but also in the organisation and efficiency of their respective Land Registries.

In Germanic systems, the Land Registry is designed as a register of title. The Land Register has a fundamental role to play in transactions over immovable goods, as inscription in the Registry has replaced the 'traditio' or the act of handing over the physical possession of the property. In Germany itself, inscription in the Land Registry has to be preceded by an agreement over the act of transferring the property (abstracted from the separate agreement over the obligations of the parties). In Switzerland, however, the law (Swiss Civil Code, ZGB) requires a causal contract that has the specific aim of transferring ownership.[12] In both systems inscription is necessary, as without inscription neither the agreement to transfer property nor the causal contract produce the effect of transmission.

In other European countries the Land Register is organised as a register of deeds. There are several types of register of deeds, some of them are simple, rudimentary collections of unorganised deeds like the ones

[11] In the words of Lange, 'Rechtswirklichkeit', n. 8, p. 226: 'Ich habe deshalb stets gegen das Abstraktionsprinzip gekämpft und halte diesen Kampf auch heute noch aufrecht, obwohl ich die Begründung aus der Unvollstümlichkeit dieses gebildes heraus nicht mehr für zuttreffend halte.' ('That is why I have always fought against the abstraction principle and I maintain this fight even today, although I do not longer consider right the justification of the elimination of this institution').

[12] ZGB, 10 December 1907, SR 210, RS 210, arts. 657 (1) and 665 (1) (Switz.).

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that exist in many parts of the United States. Nevertheless others are well organised, improved like the French, the Scottish or the Dutch Registers.[13]

2.2 *The Demand for Title Registration: An Economic Approach*

According to the way in which Registers are organised and the degree of effectiveness attributed to them, it is possible to divide them into two main categories:

(A) *The registration of deeds system*. This type of system is also termed the 'opposability system' and is currently used in France, Belgium, Portugal and Italy. The defining characteristic of this system is that documents are registered without the identification of the latest genuine title-holder, that is to say the documents are not examined beforehand as part of a process to establish the identity of the title-holder, but merely have to comply with certain formal requirements. The content of the Register, therefore, only defines a group of possible title-holders, and holds a complete set of all the documents pertaining to a property, which may be inspected on request.

Given the resulting lack of certainty of this system in some countries, as in the United States, it is quite common that subjects contract 'title insurance' to provide them with an indemnity should they be dispossessed of their title. The negative aspect of this measure is that while the indemnity provides economic security, an insurance contract obviously does not provide any degree of legal security, as the acquirer of the property may lose his title to it. Even the measure of economic security provided is limited, as the title security does not cover the full value of the property, but only the purchase price (or a percentage of the purchase price) and not any other related costs of the purchase. The payment of any indemnity is also subject to the exceptions and conditions stipulated in the insurance policy.

(B) *The registration of titles system*. This is also referred to as 'the presumption of correctness system'. This system is currently in place in Germany, Austria, Switzerland, Spain and England. In this system, rights are inscribed in the Registry, and it does not consist of a collection of original documentation pertaining to the property, as does the registration of deeds system. The Registrar is responsible for carrying

[13] Rowton Simpson would also consider them as 'title registration'. Stanhope Rowton Simpson, *Land Law and Registration* (Cambridge University Press, 1976), p. 22.

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out a check on the legality of the claims presented and will not permit any inscription that contradicts a right already inscribed in the Registry without the prior authorisation of its title-holder. In this system the principles of exactness (the content of the Registrar is presumed to be a true reflection of the legal situation) and priority (by which a posterior but registered act prevails over a previous but unregistered act) both apply.

Under the registration of deeds system, courts resolve disputes by adjudicating property rights according to the moment in which the deeds were inscribed in the Register. This creates a strong incentive for subjects to inscribe the deeds to a property as soon as possible and for the parties or their intermediaries to gain the consent of the title-holders of the rights affected in order to do so. In this way, the parties can voluntarily avoid possible future conflicts over the ownership of titles.

In the registration of titles system, private contracts are also accorded priority when inscribed. However, the Registrar is accorded authority that is almost akin to that of a judge and will not inscribe a right if it negatively affects one previously inscribed, unless the title-holder gives his permission for the Registrar to do so. This eliminates a potential weakness of the Registry and means that those legal systems that have this type of Registry treat inscription as conclusive proof of the existence of the right, and establish a system of responsibility for those exceptional cases in which there is an error in the Register. As a consequence, those who acquire a property in good faith, trusting in the accuracy of the Registry, will not be stripped of their rights over the property even if the genuine title-holder subsequently appears.

The two Registry systems incur different types of expenses and provide different kinds of benefits in terms of reducing the costs derived from the uncertainty and the risk of losing property rights.

The registration of deeds system is certainly cheaper than the registration of titles system, but it is generally considered less effective. The lower cost of the registration of deeds system is due to the fact that the examination of the deeds to establish the legality of the rights contained in them is purely voluntary, and under these systems services to assess and insure the parties are provided by private companies. This has sometimes been cited as a benefit, because, as this system facilitates the intervention of the private sector, the resulting competition to provide services tends to minimise the cost of the services they provide.

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However, in the opinion of Arruñada,[14] these advantages are more illusory then real. The cost of voluntarily insuring a right can be as much as and sometimes even higher than the cost occasioned by the inscription of the right in the public Registry. The organisation of this type of service by the private sector may also be inefficient in economic terms as they are often provided by monopolies and are normally tightly controlled by state regulations. Both the fees of a French notary and the prices that can be charged by an insurance company in the United States are fixed by the state, and both the notary and the insurance company are subject to legislation that limits entrance to their profession and specifies the 'products' they can offer and the procedures they must follow. As a consequence, this duplication of institutions (private companies and the Deeds Registry) to provide guarantees to the parties in a property transfer is not economically efficient.

The registration of titles system requires a prior examination of the legality of the rights to be inscribed and to be carried out by a public official. This requisite obviously increases the costs of the transaction. However, by organising the property Registry in a professional manner along the same lines as the organisation of the judiciary, a high level of productivity can be achieved. This level of productivity is even higher when the Registrar earns the benefits produced by the Registry office (as is the case in Spain).

The costs of the registration of titles system are offset by the greater security it provides,[15] as it protects those who acquire property in good faith through rules that govern the responsibility for errors in the Registrar (by which subjects are compensated for losses caused by errors).[16]

3 Harmonisation of Private Law in Europe and the Land Register

Legal harmonisation in Europe is a fact; it is a reality that is inexorably in continuous development whatever the nuances and reservations we want to contemplate.[17] In the field of patrimonial law, it is perceived as

[14] Benito Arruñada and Nuno Garoupa, *The Choice of Titling System in Land*, www.econ.upf.edu/docs/papers/downloads/607.pdf (last visited 12 April 2013).
[15] According to Harold Demsetz, 'Toward a Theory of Property Rights', 57 *AER*, 347 (1967): 'this improvement in the definition of the rights in question is only efficient when the benefits associated with it are greater than the costs it generates'.
[16] Arruñada and Garoupa, *The Choice of Titling System in Land*.
[17] L. M. Martínez Velencoso, 'CESL in Court. National Courts: How Can They Keep Track?', in M. Lehmann (ed.), *Common European Sales Law Meets Reality* (Berlin: Sellier, 2015).

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