

THE RIGHTS AND DUTIES OF  
MORTGAGEES IN POSSESSION AND RECEIVERS

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1. The standard remedy of mortgagees where a residential borrower is in default is to seek possession, and sell the property. In the case of higher value and commercial properties, mortgagees look to the wider range of remedies.
2. Mortgagees have extensive rights both under the LPA 1925, the general law, and under most standard mortgage conditions. They tend to prefer to appoint receivers to avoid liability as mortgagee in possession. This is understandable, but there are some misconceptions as to the role and powers of a receiver.

**Rights and liabilities of mortgagee in possession**

3. A legal mortgagee is normally entitled to possession as soon as the ink is dry on the mortgage. A mortgagee will usually want possession in order to sell with vacant possession.
4. A mortgagee who goes into possession becomes the manager of the charged property. He thereby assumes a duty to take reasonable care of the property. This requires him to be active in protecting and exploiting the security, maximising the return, but without taking undue risks. *Silven Properties Ltd v Royal Bank of Scotland plc* [2003] EWCA Civ 1409; [2004] 1 W.L.R. 997.

5. As a result, a mortgagee who goes into possession of the mortgaged property, and thereby excludes the mortgagor from control of it, is bound to account to the mortgagor, not only for the rents and profits which he actually receives, but also for the rents and profits which, but for his wilful default or neglect, he might have received; that is, for everything which he has received, or might or ought to have received, while he continued in possession. *Downsview Nominees Ltd v First City Corpn Ltd* [1993] AC 295.
6. Thus, for example, when the property is not let, the mortgagee must use due diligence to let it, and, if it remains unlet through his default, he is charged with the rents which ought to have been obtained. The mortgagee is under no duty to let the property if a letting might hinder or interfere with an intended sale of the property.
7. In relation to property let under a lease granted on or after 1 January 1996, a mortgagee in possession is liable on the covenants in the lease, either as landlord or tenant as the case may be. Landlord and Tenant (Covenants) Act 1995 s 15.
8. These liabilities are avoided by the appointment of a receiver, who is deemed to be agent of the mortgagor.

### **Rights of receiver**

9. A receiver has statutory power to demand and recover all the income of which he is appointed receiver by bringing proceedings, by distress or otherwise, in the name either of the mortgagor or mortgagee, to the full extent of the estate or interest which the mortgagor could dispose of, and to give effectual receipts and to exercise any powers which may have been delegated to him by the mortgagee. See Law of Property Act 1925 s 109(3). The mortgage conditions usually give the mortgagee power to appoint a receiver with power to do anything the mortgagor might do and power to exercise the mortgagees powers.

10. There are, however, limitations on the receiver's powers:
- a. he cannot sell the property as agent for the mortgagor free from interests such as subsequent mortgages and leases binding on the mortgagor. The mortgagee, on the other hand, can sell free from subsequent mortgages and leases not binding on the mortgagee;
  - b. he cannot claim possession of the mortgaged property unless as agent for the mortgagee.

**General duties owed by mortgagee.**

11. A mortgagee owes duties in equity to the mortgagor and any subsequent incumbrancer or surety. The duties cannot be replaced or supplemented by a liability in negligence or extended to others such as beneficiaries under a trust of the mortgaged property. They can be excluded by agreement.
12. The mortgagee is not obliged to exercise his powers even if advised to do so, although the mortgaged property is depreciating and however advantageous it might be to the mortgagor. He can decide if and when to exercise his powers on the basis of his own interests. He is not obliged to enforce his security and may rely on the personal covenant for payment.
13. The mortgagee does, however, owe a general duty to exercise his powers in good faith for the purpose of obtaining repayment which flows from the equitable principles for the enforcement of mortgages and the protection of borrowers, that a mortgage is security for the repayment of a debt. It has been said that he owes a duty to act fairly towards the mortgagor.
14. The main recent authorities for these well established propositions are *China & South Sea Bank Ltd v Tan* [1989] 3 All ER 839, PC, *Downsview Nominees Ltd v First City Corpn Ltd* [1993] AC 295, *Medforth v Blake* [2000] Ch 86, CA and *Silven Properties Ltd v Royal Bank of Scotland plc* [2004] 1 W.L.R. 997.

15. The limitation period for a claim for breach of the duty in equity owed by a mortgagee is six years.

**General duties owed by receivers**

16. The receiver is agent of the mortgagor, but it is no ordinary agency, as explained in *Silven Properties Ltd v Royal Bank of Scotland plc*. In particular
- a. the agency is one where the principal, the mortgagor, has no say in the appointment or identity of the receiver and is not entitled to give any instructions to the receiver or to dismiss the receiver.
  - b. there is no contractual relationship or duty owed in tort by the receiver to the mortgagor: the relationship and duties owed by the receiver are equitable only: see *Medforth v Blake* [2000] Ch 86 and *Raja v Austin Gray* [2003] 1 EGLR 91;
  - c. the equitable duty is owed to the mortgagee as well as the mortgagor. The relationship created by the mortgage is tripartite involving the mortgagor, the mortgagee and the receiver;
  - d. the duty owed by the receiver (like the duty owed by a mortgagee) to the mortgagor is not owed to him individually but to him as one of the persons interested in the equity of redemption. The class character of the right is reflected in the class character of the relief to be granted in case of a breach of this duty. That relief is an order that the receiver account to the persons interested in the equity of redemption for what he would have held as receiver but for his default;
  - e. not merely does the receiver owe a duty of care to the mortgagee as well as the mortgagor, but his primary duty in exercising his powers of management is to try and bring about a situation in which the secured debt is repaid: see *Medforth v Blake*; and
  - f. the receiver is not managing the mortgagor's property for the benefit of the mortgagor, but the security, the property of the mortgagee, for the benefit of the mortgagee. His powers of management are really ancillary to that duty.

17. A receiver and manager owes the same duty in equity to the mortgagor, all subsequent incumbrancers and guarantors as the mortgagee to exercise his powers in good faith and for the purpose of obtaining repayment of the debt owing to the mortgagee. In a number of respects, however, a receiver is in a very different position from a mortgagee: whilst a mortgagee has no duty at any time to exercise his powers to enforce his security, a receiver has no right to remain passive if that course would be damaging to the interests of the mortgagor or mortgagee. In the absence of a provision to the contrary in the mortgage or his appointment, the receiver must be active in the protection and preservation of the charged property over which he is appointed. Thus if the mortgaged property is let, the receiver is duty bound to inspect the lease and, if the lease contains an upwards only rent review, to trigger that rent review in due time. His management duties will ordinarily impose on him no general duty to exercise the power of sale. But a duty may arise if e.g. the goods are perishable and a failure to do so would cause loss to the mortgagee and mortgagor.
18. He does not owe the mortgagor any duty comparable to the duty owed to a company by its own directors or managers. He is entitled, but not bound, to allow the company's business to be continued by himself or by the existing or other executives. The decisions of the receiver and manager whether to continue the business or close down the business and sell assets chosen by him cannot be impeached if those decisions are taken in good faith while protecting the interests of the debenture holder in recovering the moneys due under the debenture, even though the decisions of the receiver and manager may be disadvantageous for the company. The duties owed by a receiver and manager do not compel him to adopt any particular course of action, such as selling the whole or part of the mortgaged property, carrying on the business of the company or exercising any other powers and discretions vested in him. The primary duty of the receiver is to the debenture holders and not to the company. If the receiver does decide to carry on the business, he owes a duty to take reasonable steps to do so profitably. See *Gomba Holdings Ltd v Minorities Finance Ltd* [1988] 1 WLR 1231, CA; *Downsview Nominees Ltd v First City Corp'n Ltd* [1993] AC 295; *Routestone Ltd v Minorities Finance Ltd* [1997] BCC 180; *Medforth v Blake* [2000] Ch 86, CA; *Silven Properties Ltd v Royal Bank of Scotland plc* [2004] 1 W.L.R. 997.

**Exercise of power of sale by mortgagee**

19. A mortgagee is not obliged to exercise the power of sale even if advised to do so, or if the asset is depreciating, however advantageous a sale might be to the mortgagor. By the same token, he is not obliged to delay in the hope of obtaining a higher price, if redemption is imminent or until after the pursuit of an application for planning permission or the grant of a lease of the mortgaged property, though the outcome of the application and the effect of the grant of the lease may be to increase the market value of the mortgaged property and price obtained on sale. A mortgagee is entitled to sell the property in the condition in which it stands without investing money or time in increasing its likely sale value. He is entitled to discontinue efforts already undertaken to increase their likely sale value in favour of such a sale. He can decide if and when to sell on the basis of his own interests.
20. He owes a duty in equity to exercise the power in good faith for the purpose of obtaining repayment and to take reasonable precautions to secure a proper price. The duty is not breached by a mortgagee's assessment of the market value of the mortgaged property which falls within an acceptable margin of error.

**Exercise of power of sale by receiver**

21. A receiver exercising his power of sale also owes the same specific duties as the mortgagee. The receiver is entitled (like the mortgagee) to sell the property in the condition in which it is without awaiting or effecting any increase in value or improvement in the property. The receiver is not obliged before sale to spend money on repairs, to make the property more attractive before marketing it, or to "work" an estate by refurbishing it or to apply for planning permission.

**Recent examples of complaints about the exercise of a power of sale.**

22. In *Silven Properties Ltd v RBS* [2004] 1 WLR 997, the complaint was that the receivers should not just have sold the property, but sought planning permission and granted leases of two vacant units before selling to realise the best price. The claim was dismissed. It was held by the Court of Appeal that the receiver was under no greater duty than a mortgagee, notwithstanding the conceptual difference in their roles.
23. In *Bell v Long* [2008] EWHC 1273 the receiver had four properties to sell. Weatheralls advised that they should be advertised separately. They received offers for 3 amounting to £630,000, and the fourth had been valued at £325,000. Weatheralls recommended a change of strategy, and sold all four together for £775,000. They were all resold for £1.12m. The complaint was that the properties should have been sold separately as originally planned, that they were not adequately marketed separately, and that they were in fact worth £1.12m as demonstrated by the subsequent sale. The complaints were rejected, as based on hindsight. It was held that the receiver had acted reasonably on the basis of the information he had at the time. It was reasonable to proceed with a portfolio sale, notwithstanding the fact that it would attract a discount of 10-15%, given the uncertainties as to whether the fourth property would be sold. The expert evidence was not reliable as it was based principally on evidence of subsequent transactions. The question was not what the properties were worth on the basis of comparable transactions, but had the receiver acted reasonably. He had.

## Human Rights

24. There was a brave attempt last year to argue that a sale by a receiver without obtaining an order for possession was a breach of the borrower's human rights. See *Horsham Properties v Clark* [2008] EWHC 2327. The purchaser claimed possession from the borrowers. They had no defence, and could not rely on s36 of the Administration of Justice Act 1970. It was argued that the sale was pursuant to s101 LPA 1925, and that the property was a possession of which the mortgagors were unjustifiably deprived by the sale because they could not invoke the courts discretion to postpone a sale under s36 AJA. Not surprisingly the argument was rejected because
- a. the sale was pursuant to essentially contractual powers, not statute. A1P1 was not engaged;
  - b. alternatively, the ability of a mortgagee to sell without seeking possession was clearly justified in the public interest;
  - c. furthermore, s101 could not be read as requiring a mortgagee to seek possession first.

## Variation of interest rates

25. In the current market variable interest rates vary widely from lender to lender. The question arises whether there are any limitations on the right to vary a rate, or to impose different rates for different customers. This issue arose in *Paragon Finance v Nash and Staunton* [2002] 1 WLR 685, CA and again in *Paragon Finance v Pender* [2005] 1 W.L.R. 3412, CA.
26. The cases arose from the decision of Paragon to withdraw from the mortgage market, and raise its rates until they were 4% above the variable rates of Halifax. The borrower sought to argue that they were unreasonably high. The Court of Appeal held that the power to vary interest rates was subject to an implied qualification that it will not be exercised improperly, capriciously or arbitrarily, or in a way which no reasonable mortgagee, acting reasonably, would do.

27. It was held that it was not improper or unreasonable for the mortgagee to raise rates to deal with its own financial difficulties. An example of an improper purpose was a case where: “... *the lender decided that the borrower was a nuisance (but had not been in breach of the terms of the agreement) and, wishing to get rid of him, raised the rate of interest to a level that it knew he could not afford to pay.*”
28. It was held in *Pender* that a lender could, for a genuine commercial reason, adopt a policy of raising interest rates to levels at which its borrowers generally, or a particular category of its borrowers, may be expected to consider refinancing their borrowings at more favourable rates of interest offered by other commercial lenders.
29. It was also not a breach of the implied term for a lender to raise rates for ‘old book’ borrowers, to enable the lender to offer better rates for recent borrowers. It was perfectly legitimate for the lender to adopt that policy to help recover itself from the losses that it has sustained over a period of time.

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