70317
REAL PROPERTY

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Textbooks: Moore; Real Property, Oxford University Press, 3rd, 2012, AND
Gray, Edgeworth, Foster and Dorsett; Property Law in N.S.W, Lexus Nexus, 3rd., 2012

COMPREHENSIVE EXAM NOTES WITH ALL THE CASES AND DETAILED INFO

TOPICS 1-3 ARE NOT EXAMINABLE BUT ARE ATTACHED AT THE END OF THESE NOTES FOR REFERENCE

UNIVERSITY OF TECHNOLOGY SYDNEY
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70317 – REAL PROPERTY
(Lectures with Shaunnagh Dorsett and Geoffrey Moore)
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TOPIC 4: MORTGAGES

Under OLD SYSTEM TITLE:

- A first mortgage by deed takes the form of a conveyance (meaning it passes the legal estate) to the first mortgagee. Although the mortgagee becomes the legal owner of the land, the mortgagor retains the right to have it reconveyed – conditioned upon full payment of the debt.
- The mortgagor's equitable interest upon discharge of the mortgage is called "Equity of Redemption"
- A second or subsequent mortgage is in essence a mortgage of the mortgagor's equity of redemption. – The equity of redemption is itself an estate in land. It is a proprietary right which can be conveyed, leased, or mortgaged.

NOTE: Although under OST mortgages are in a form of transfer, there may still be unregistered equitable mortgages: (All except the last one are unregisterable)

- An equitable mortgage by deposit of title deeds (by conduct):
    - *Cooney v Burns* (1922) 30 CLR 216; Theodore v Mistford (2005) 221 CLR 612
- An agreement to grant a mortgage:
    - *ANZ Banking v Widin* (1990) 26 FCR 21
- Ineffective attempt to create a legal mortgage – non-compliance with formalities of a deed.
    - Swiss Bank v Lloyd Bank [1982] AC 584
- A written mortgage simply not registered (but must be in writing: s 23C of the CA or supported by sufficient acts of part performance: s 23E of CA)

Equity of Redemption

- The Equity of Redemption is the entitlement of the Mortgagor in equity to have his/her property reconveyed once the debt has been redeemed in full. (Santley v Wilde (1899))
- The duration of the Equity of Redemption is the combined period of:
    - contractual right to redeem (before expiration or before default) + the equitable right to redeem.
        - The equitable right to redeem come to an end when the mortgagee either sells or forecloses the mortgaged property.
    - Upon default, bank/mortgagee can get an order of possession to exercise its options.

Foreclosure (Conveyancing Act ss. 99A, 100)

- A mortgagee is entitled to foreclose and become the owner of the mortgaged property
    - *Kreglinger v New Patagonia Meat* [1914] AC 25
- Foreclosure is where the mortgagee becomes the owner of the property. The mortgagee exchanges the debt for ownership of the mortgaged property
- Steps to obtain an order of Foreclosure (OST/unregistered Torrens Mortgages)?
    1. Default
    2. Statutory Notice to remedy default within 30 days: s 111 *of CA*
    3. Non-compliance with the notice
    4. Properly conducted auction: s 99 of CA
    5. Highest bid is less than the debt owed: s 99A of CA
    6. Application for Foreclosure the Court
    7. Further period given to mortgagor to repay
    8. Order for Foreclosure made absolute

<u>MORTGAGES UNDER TORRENS</u>

- A registered mortgage of land is a statutory charge and not a conveyance of the land (s 57 RPA)
- The mortgagee obtains indefeasibility upon Registration.
- The mortgagor's interest is more than an equity of redemption – the mortgagor remains the registered proprietor of the land.

POWERS OF A MORTGAGEE

1. Foreclosure
    - ss 61 and 62 of the RPA
    - Pre-requisites:
        1. Default
        2. Statutory Notice to remedy default within 30 days: s 57 RPA
        3. Non-compliance with the notice
        4. Properly conducted auction: s 61 RPA
        5. Highest bid is less than the debt owed: s 61 RPA
        6. The Register-General must issue foreclosure order or require applicant to offer land for sale and issue order after failed to be sold or price insufficient: s 62 RPA
        7. Further period given to mortgagor to repay (usually 6 month)
        8. RG records the foreclosure order in the register: s 62(3) RPA
2. Right to sue on a personal covenant
    - Sue mortgagor for any default under the contract.
    - This is personal, and does not run with the land. Only the original mortgagor, his personal representatives in case of death, will be liable.
3. Right to Possession
    - Under OST – legal estate passes to mortgagee thus has the right to possess even without default, but impliedly excluded so long as there is no breach.
    - Under Torrens – mortgagor is entitled to retain possession until default. From default, statute confers a right of possession to mortgagee: s. 60 RPA.
4. Right to appoint a receiver to collect rents
    - s 100, 115A, 109(1)(c), 109(5) of CA
5. Right to Improvement of property
    - If mortgagee is in possession, he can spend money to improve the property to ensure it is in saleable condition: Matzner v Clyde
    - However, the improvement must not change the character of the property, and mortgagee should ensure that the expenditure enhances the value of the property and was justifiable: *Southwell v Roberts* (1940) 63 CLR 581

6. MORTGAGEE SALE

- OST - CA, ss 109, 111, 111A and 112;
- Torrens – RPA, ss 57, 58, 58A and 59
- This remedy is preferred than foreclosure because it is easier and simpler in procedure, and there is a chance to recover shortfall between sale price and amount of security.

PREREQUISITES FOR MORTGAGEE SALE

1. Default
2. Statutory notice requiring default to be remedied within 30 days (s 57 RPA; s 111 CA)
3. Non-compliance with notice

WHEN IS A SALE VALID?

a. A sale is necessary. A mortgagee cannot sell to himself: *Farrar v Farrars Ltd* (1881) 40 Ch D 395
b. When selling to a related entity there must be a truly independent bargain: *ANZ v Bangadilly Pastoral* (1978) 139 CLR 195
c. Once the three prerequisites have occurred it is the mortgagee's call as to if and when he/she will sell: *Belton v Bass, Ratcliffe* [1922] 2 Ch 449 (Cf. *Palk v Mortgage Services* [1993] 2 All ER 481)

CASES:

- *Farrar v Farrars Ltd* (1881) 40 Ch D 395
    - A sale by a mortgagee to a company of which he was a director and shareholder was held to be valid and effective to extinguish the equity of redemption, but only because the sale was negotiated between the mortgagee and the other directors at arms' length. A sale by a mortgagee to a company of which he was sole director and only shareholder would be ineffective. A power of sale does not authorise the donee of the power to take the property at a price fixed by himself. If the sale is unauthorised, it cannot affect the beneficial interests.

- *ANZ v Bangadilly Pastoral* (1978) 139 CLR 195
    - The mortgagee and the purchasing company had common directors. The sale between the first mortgagee to the purchaser was a sale between two related entities. As the sale was one with a related entity, the court held that the parties to the contract must satisfy the court that there was a truly independent bargain.

- *Belton v Bass, Ratcliffe* [1922] 2 Ch 449

- The mortgagees of shares in a brewery wanted to a director to be able later to acquire the shares. They could not grant an option. They sold the shares to the director, as mortgagees, and lent the purchase price, interest free. The director could require the mortgagees to buy back the shares at the original purchase price. The result was as if they had granted an option. The mortgagor sought to have the transactions set aside, arguing that: ' . .it is said that the mortgagee exercised his power of sale with an indirect motive, not with the view of realizing his security, but with the object of conferring a benefit upon the defendant by giving him an option masquerading as a sale.' But the court held that it is not to inquire about the mortgagee's motive as it is his call if and when she wants to sell.
- Held: Russell J said: 'I am unable accordingly to inquire into the motives of the defendants Bass, or to hold that the sale is vitiated because they desired to confer a benefit on the purchaser by selling to him upon terms, which included a fair price.'

- *Palk v Mortgage Services* [1993] 2 All ER 481
  - The mortgagees had obtained an Order for possession with the intention, not of proceeding to sell the property but of waiting in the hope that the market might improve. The mortgagor was anxious that the property should be sold so that the proceeds would reduce the mortgage debt, on which interest was accruing at an alarming rate.
  - Held: Since the mortgagees could buy the property themselves if they wished to speculate on an increase in its value, in the interests of fairness the property should be sold. The duty to take reasonable care of the property secured requires the mortgagee to be active in protecting and exploiting the security, maximising the return, but without taking undue risks. In such a case the mortgagor might obtain an order for sale even though the proceeds of sale would be insufficient to discharge the mortgage debt.
  - Nicholls V-C said: 'I have given two examples where the law imposes a duty on a mortgagee when he is exercising his powers: if he lets the property he must obtain a proper market rent, and if he sells he must obtain a proper market price. I confess I have difficulty in seeing why a mortgagee's duties in and about the exercise of his powers of letting and sale should be regarded as narrowly confined to these two duties. In addition to the mortgaged property, a mortgagee normally has a right of recourse against the borrower personally. He may also have the benefit of a guarantee from a third party. There is no problem when the borrower or guarantor can raise the necessary money, or the security available is adequate and readily realisable. Then the borrower should arrange to pay off his debt in full. The difficulty arises when that is not possible. Then the borrower is in the mortgagee's hands. Whether in that situation a mortgagee is at liberty to exercise his rights of leasing and sale in a way that in all likelihood will substantially increase the burden on the borrower or guarantor beyond what otherwise would be the case is not a question I need to decide on this appeal . . That he should act in such a cavalier fashion is not a proposition I find attractive. That is a question which may call for careful examination on another occasion . .'

MORTGAGEES OBLIGATIONS WHEN SELLING

Earlier approach

- Earlier cases were split between an approach based on bona fide (i.e. acting in good faith) and taking reasonable steps to obtain reasonable price.

NOW:

- Statutory duty to <u>take reasonable care</u> to obtain best price: S. 111A has legislated the latter approach
  - Section 111A of the Conveyancing Act requires a mortgagee when selling to "take reasonable care to ensure … the best price that may reasonably be obtained in the circumstances"
  - Sub-s (8) provides that s. 111A of the Conveyancing Act applies to RPA/Torrens mortgages.
  - This is a question of fact.
- Corporations Act s. 420A :
  - Section 420A provides that in exercising a power of sale in respect of property of a corporation that has a market value, a controller must take all reasonable care to sell the property for not less than that market value.
  - The requirement imposed operates cumulatively to the obligation to act in good faith which otherwise exists under the common law.

What is 'REASONABLE CARE?'

McHugh v Union Bank of Canada [1913] AC 299

- There was a mortgage of horses, which the mortgagee needed to drive to market if he was to sell them.

  Held: If a mortgagee goes on with a sale of property which is unsaleable as it stands, a duty of care may be imposed on him, when taking the necessary steps, first to render the mortgaged property saleable. The mortgagee owed to the mortgagor a duty to take proper care of the horses whilst driving them to market. The duty imposed on the mortgagee was to take care to preserve, not increase, the value of the security.

Cuckmere Brick v Mutual Fin. [1971] 1 Ch 949

- A mortgagee exercising the power of sale advertised the property for sale as having planning approval for the building of houses on the property. In actual fact, the mortgagor had obtained planning approval to build flats as well as housing. The mortgagor drew the omission to the attention of the mortgagee but the sale proceeded anyway. The purchaser of the property bought the property to develop houses and paid £44,000. Evidence presented to the court demonstrated that if developers interested in building flats had been aware of the planning approval, the property could have sold for around £65,000 to a developer of flats. Evidence also demonstrated that the omission in advertising was not dishonest or intentional. Had the mortgagee breached any obligations to the mortgagor in selling in this way?
- A mortgagee selling as mortagee in possession must 'take reasonable care to obtain the true value of the property at the moment he chooses to sell it' and obtain the best price for the property reasonably obtainable on the open market.
- Salmon LJ said: 'No doubt in deciding whether he has fallen short of that duty the facts must be looked at broadly, and he will not be adjudged to be in default unless he is plainly on the wrong side of the line'.
  It is not a duty breach of which is actionable without proof of damage. In default of provision to the contrary in the mortgage, the power of sale is conferred upon the mortgagee by way of bargain by the mortgagor for his own benefit and he has an unfettered discretion to sell when he likes to achieve repayment of the debt which he is owed. There is no obligation on a mortgagee to delay a sale in order to get a higher price, and the best price reasonably possible does not necessarily equate with true market value.
- Cross LJ said: 'A mortgagee exercising a power of sale is in an ambiguous position. He is not a trustee of the power for the mortgagor, for it was given him for his own benefit to enable him to obtain repayment of his loan. On the other hand, he is not in the position of an absolute owner selling his own property but must undoubtedly pay some regard to the interests of the mortgagor when he comes to exercise the power.
  Some points are clear. On the one hand, the mortgagee, when the power has arisen, can sell when he likes, even though the market is likely to improve if he holds his hand and the result of an immediate sale may be that instead of yielding a surplus for the mortgagor the purchase price is only sufficient to discharge the mortgage debt and the interest owing on it. On the other hand, the sale must be a genuine sale by the mortgagee to an independent purchaser at a price honestly arrived at.'

ANZ v Bangadilly Pastoral (1978) 139 CLR 195

- property was sold at an auction that was held on 23 December after being advertised only once in the metropolitan paper (not where the land was nor the auction was to be done). Further, the mortgagees told the auctioneers to set the reserve price at $250 000 and Bangadilly Pastoral were successful with a $265 000 bid.
- Second mortgagee was not informed of the auction sale.
- The sale was set aside as it was not the result of an independent bargain since the transaction came about primarily through the deciding minds of the mortgagees, with the auction not being timed and advertised to best attract potential buyers. It was also sold to a close associate of the vendors, with Bangadilly Pastoral having been set up just eight days before the auction which had the same directors and members.

REASONABLE CARE + AGENT'S CONDUCT

Pendlebury v Colonial Mutual Life Assurance Society (1912) 13 CLR 626

- Mortgagee sold a block of acres of land in northwest Victoria. The land was to be sold by auction in Melbourne and was advertised in 2 newspapers. The ad paid little regard to certain features of the property. Mortgagor complains that the mortgagee was not exercising reasonable care when the auction was conducted under circumstances that preclude fair competition for the land was worth 2000pounds but was sold only at 720pounds, and there was collusion between the purchaser and an employee of the mortgagee.
- Held: the mortgagee must not recklessly or willfully sacrifice the interest of the mortgagor and that if he does he is in bad faith. It is not disputed that some advertisement is necessary. But this ad must be wide extensive and complete to obtain fair sale.
- The mortgagee is also liable on the agent's conduct.
- Barton J: the duty to act in good faith necessarily includes observing reasonable precautions to obtain a proper price.

CAGA v Nixon (1981) 152 CLR 491

- CAGA exercised the power to sell. CAGA employed a firm of real estate agents to conduct the sale by auction and instructed them to advertise the sale in The Courier-Mail. The one ad published in the newspaper was unsatisfactory in so many ways.
- Because the auction was insufficiently advertised, there was a failure to take reasonable care to ensure that the property was sold at its market value.

- Although CAGA was not itself directly responsible for the insufficient advertising as it left the matter to agents whom it had chosen, the mortgagee would be liable on its agent's conduct.
- Although a mortgagee is not a trustee of the power of sale for the mortgagor, he is not entitled to sacrifice his interest in conducting the sale.
- Although appellant took reasonable care to choose competent agents and left the conduct of the sale in their hands, this does not mean that they are discharged in its duty. The duty is not merely to take care to ensure that the sale is carried out by competent agents, but reasonable care to ensure that the property is sold at the best price.

REMEDIES TO AN IMPROPER SALE

- Pre-exchange – a mortgagor must pay total debt into court to restrain a sale
  - *Inglis v Commonwealth* (1972) 126 CLR 161

- Between exchange and settlement, the court may restrain a mortgagee sale on terms:
  - *Harvey v McWatters* (1948) 49 SR (NSW) 173;
  - *Brutan Inv v Underwriting* (1980) 39 ACTR 47

- After settlement, a mortgagor's complaint is confined to damages and the sale proceeds
  - UNLESS the purchaser was a party to the impropriety
    - *Latec Inv. v Hotel Terrigal* (1965) 113 CLR 265
      - mortgagee sold to a subsidiary company with fraud by financing to a third party.

  Allfox v Bank of Melbourne (1992) NSW ConvR 55-634
  - The general rule is that a mortgagee will not be restrained from exercising a power of sale merely because the amount due is in dispute, or because the mortgagor has commenced a redemption action, or because the mortgagor objects to the manner in which a sale has been or is being arranged. The mortgagee will only be restrained if the mortgagor pays the amount claimed to the Court unless, on the terms of the relevant mortgage, the claim is clearly excessive (inglis and Harvey cases see above)
  - Exception to the general rule:
    - Validity of mortgage in issue
    - Availability of power of sale is in issue
      - Challenge on breach of covenant
      - Irregularity in exercising power of sale
  - Injunction may be required to prevent interference with rights – if challenge on the grounds of validity of mortgage and non-existence of power of sale
  - BUT if based on imporper exercise of duty, above rules will govern as to time and remedy.

PENALTY CLAUSES

S 93 CA

- In some mortgage contract, there will be clauses where a mortgagee will impose a penalty when the mortgagor opts to pay the debt right away.
- HOWEVER, Conveyancing Act, s 93 provides: regardless of what the mortgage contract says, a borrower can pay the debt early without any penalty BUT should still pay the interest due for the entire period.
- S 93 only applies when the mortgagor elects to pay early. This does not apply when the mortgagee demands the early payment.

CASES:

Potter v Edwards (1957)
- Parties may agree that the mortgagor will pay a premium over and above the sum advanced however, when this premium is conditional upon there being default, equity regards this a s an unenforceable penalty.
- TEST: look if payment is linked to default = penalty

Strode v Parker (1694) 32 ER 804
- Someone lending money increased the interest rate once borrower defaulted.
- TEST: default + increase in rate and applied retrospectively = penalty

Securities v CBA
- Mortgagee raises interest rates prospectively because of the default = penalty

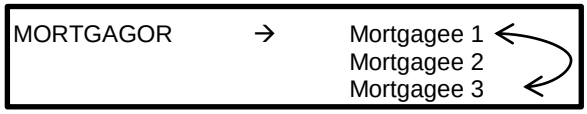
Wanner v Caruana [1974] 2 NSWLR 301; O'Dea v All States Finance (1983) 152 CLR 359
- A mortgage provided for interest at 10% reducible to 9% per annum, with the whole principal and interest to be repaid over 6 yrs. On default, it became due and payable, the whole of the principal then outstanding, plus interests at 10% for the whole balance of 6 yrs.
- 2 questions to be asked when assessing whether a term is a penalty:
  - Genuine pre-estimate of loss
  - Term grants damages that is disproportionately large.

- In this case, the Mortgagee offered a discount on a high interest rate. Upon default, the loan is demanded back at the original higher rate.
    - If it was at a discounted rate: it would not be a penalty.
    - If at the original (higher) rate: not a penalty
    - If including all future interest = penalty (Because the mortgagee demanded immediate early repayment, it would be a penalty. Interest would only be up until repayment.)

TACKING

- this involves priority of interest of 2 or more mortgagees in one property.

I. *Tabula in Naufragio*
- literally: "Grabbing hold to a financial shipwreck"
- This is where a 3rd mortgagee buys out the 1st mortgagee to gain priority, or M1 assigns his interest to M3.



RULE: If M3 took assignment of M1 AND had NO NOTICE of M2, then M3 could tack on M1 to prevail over M2. (Taylor v Russel [1892] AC 244)

II. Further Advances by First Mortgagee

RULES:
- If A made further advancements with notice of B, A cannot tack on his M3 on his M1
    - *Hopkinson v Rolt* (1861) 11 ER 829
- This will be so regardless if they are contractually bound to lend more money
    - West v Williams [1899] 1 Ch 132
- Actual notice will defeat tacking
    - Re O'Byrne's Estate (1885) 15 LR (Ir) 189
    - *Westpac v Adelaide Bank* [2005] NSWSC 517
        - Adelaid bank lent money to X, Westpac lends X money to pay Adelaide bank
        - Adelaide bank lend another sum of money to X after this.
        - Held: Adelaide bank having been paid out by Westpac of X's previous advances serves as adequate notice that Westpac is a mortgagee. Knowing such, it would be personal equity/fraud if they will not be subject to that mortgage.
- Where A's mortgage does not provide for further advances, nor does it provide more generally that the security secures both initial and any further advances, then A will only prevail over B where A had no notice of B – whether actual, constructive or imputed notice.
    - *Credland v Potter* (1894) LR 10 Ch App 8

XPT: THE MATZNER EXCEPTION based on justice, proportionality and unconscionabilty

Matzner v Clyde [1975] 2 NSWLR 293

- According to Holland J, the rules applicable to OST also apply to Torrens mortgage.
- BUT the facts of this case is what made it have a different outcome
- Developer got approved to build 24 apartments and is to complete work in stages. They secured an advance on M1 with agreements of further advances. For its next stage, developer secured money from M2. However, developer ran out of money and the project was half-built. M1 was concerned about this for it would diminish the value of the property as it was half built. M1 then lent more money for its completion with notice of M2 with the view of improving the property's value for sale.
- HELD: on first assessment, M1 can only avail the amount up to the one agreed initially following the above rules. However, Justice Holland found that because this rule is about being fair to the later mortgagees, if the value of the security is increased by the further advances, then it cannot be unfair to them to allow the further advances to take priority:

- "I can see no grounds for denying to the mortgagee first priority for advances made pursuant to … the mortgage .. up to the total amount of the principal sum .. on the basis of justice and fair dealing between the parties. Advances made under those clauses after notice of the subsequent mortgages were not designed or liable to diminish the value of the security given to the subsequent mortgagees".

BUT: improvements must be reasonable

Southwell v Roberts (1940) 63 CLR 581

- In Southwell v Roberts (1940) 63 CLR 581 a mortgagee entered into possession of property after a default by the mortgagor. After some years as mortgagee in possession, the mortgagee determined that the properties had become so dilapidated that it was not possible to economically repair them and accordingly decided to demolish and rebuild the houses. This work was carried out and resulted in two semi-detached brick cottages being constructed on Portion "A" and a double fronted detached brick bungalow being constructed partly on Portion "A" and partly on Portion "B".
- Mortgagee spent nealry double the mortgage liability
- Starke J. said : In my opinion the amount expended was neither reasonable in amount nor reasonable having regard to the nature of the property. The mortgagee expended double the amount of the principal debt and changed the character of the buildings upon the land, and indeed on the vacant portion of the land she erected a building where none had been before. The case is an example of a mortgagee in possession effecting improvements without regard to the mortgagor's interest and calculated to improve him out of his property. In these circumstances the expenditure cannot be allowed, unfortunate though it be for the mortgagee. But she could have protected herself by obtaining the consent or acquiescence of the mortgagor or possible by fore-closing.

SUMMARY OF RULES ON TACKING

Under OST

a) When M3 had no actual or constructive notice
b) When M3 had no actual notice and there was an initial provision for further advances.
c) When it is against conscience for M2 to deny that M1(as M3) is entitled (Matzner facts)

Under TT

a) When M3 had no actual or constructive notice
b) When M3 had no actual notice and there was an initial provision for further advances.
c) When it is against conscience for M2 to deny that M1(as M3) is entitled (Matzner facts)
d) Arguably also when M1 is registered and has an indefeasible right to all money, whenever lent.

Might be able to classify further advance as a reasonable improvement to the property
(cf Southwell v Roberts)