WHOSE AGENT ARE YOU ANYWAY?

Tricia Hemans and Roisin McGlinn consider common arguments raised by borrowers against LPA Receivers

When a borrower enters into default lenders will make every attempt to resolve matters without recourse to court proceedings. However, there will sometimes come a point where steps need to be taken to enforce the security which the lender has. The usual remedies considered will be possession, sale and the appointment of a receiver.

Appointing a receiver is an attractive remedy for lenders given that the receiver acts as the agent of the mortgagor and not the mortgagee, provided the relationship is managed correctly. However, if the lender directs the receiver or takes some other step in relation to the mortgaged property suggesting that they are in fact a mortgagee in possession, the agency may be pierced. Unless the mortgage deed specifies some other arrangement, it is the borrower who will be solely responsible for the receiver's acts or defaults and any issues which arise with the property. Therein lies the first challenge often brought by aggrieved borrowers: how could it possibly be right that the lender appoints a receiver who is the agent, not of the lender that appoints him, but rather the borrower who would have had nothing to do with the appointment?

At first blush, one might sympathise with the thought. After all the lender will appoint a receiver to protect his own interests and there is no duty of care owed to the borrower in making the selection, nor is there any duty of care towards other creditors for that matter (see: *Re Potters Oils (No.2)* [1986] 1 W.L.R. 201 at 206 and *Downsview Nominees Ltd* v *First City Corp Ltd* [1993] A.C. 295 at 312).

In addition, the primary duty of the receiver is to the mortgagee that appointed him and not the mortgagor. Despite the relationship of agency that the appointment creates between the borrower and receiver, the receiver can act in a way which disadvantages the borrower. However, it should be noted that there is duty to act in good faith. A lender who, for example, appointed a receiver knowing that the receiver intended to exercise his powers for the purpose of frustrating the activities of the second mortgagee may well be in breach of his duties. A receiver must also exercise his powers in good faith and for the purposes of obtaining repayment of the debt owed to the mortgagee.

Despite the complaints and challenges frequently raised by borrowers, section 109(2) Law of Property Act 1925 ("**LPA**") makes it clear that a receiver appointed under the statutory powers is deemed to be agent of the mortgagor. The justification for this is simple. In signing the mortgage, the borrower has agreed that, in certain pre-agreed circumstances, the lender will have the right to appoint a receiver who will act as the borrower's agent. A receiver cannot be appointed unless any preconditions set out in the mortgage contract are satisfied. This typically requires some breach of the payment or other provisions of the deed. Under statute a receiver cannot be appointed unless the mortgage money has become due (under section 101(1) LPA), and the power of sale has become exercisable. By section 103 LPA this will not be the case unless a notice of default has been served, two months' arrears of interest have accrued or some other covenant has been breached. As such, the appointment of a receiver is only possible where the borrower has failed to comply with his obligations in some way. The agency relationship created is a device by which the mortgagee is protected as the receiver's main objective will be to bring about a situation whereby the secured debt is repaid.

After the principle of agency is challenged, borrowers will next seek to attack the powers conferred on the receiver as a result of that agency. Section 109(3) LPA makes clear that the receiver appointed under statute has the power to demand and recover income, bring proceedings in the name of either the borrower or lender and to exercise any powers which may have been delegated to him by the mortgagee. Given the limited powers conferred by statute it is very important for lenders to have clear mortgage conditions setting out the extended powers of the receiver.

Whilst the receiver will usually contact the tenant or occupiers of the borrower's property to explain the practical effect of the receiver's appointment, it is not uncommon for a borrower to tell the tenant to ignore this correspondence and direct that rent should still be paid directly to the borrower. However, once the receiver has been appointed, the borrower cannot validly receive money as for rent and therefore the receiver could in fact treat any non-payment by the tenant as rent arrears, even though the tenant has already paid the sum due to the borrower. This is something which will be more common where the rent is well in excess of the contractual mortgage payments due, or indeed situations where the borrower is

not making any payment towards the mortgage at all and is simply using the rental income for other outgoings.

The receiver's powers also include the power of leasing and accepting surrenders which by section 99(19) LPA displaces the borrower's right to do so. Any tenancy purportedly granted by a borrower after the appointment of a receiver will therefore be of no effect. In addition, following the Court of Appeal decision in *McDonald and McDonald* [2014] EWCA Civ 1049 (which went to the Supreme Court but on another point), it is clear that where the mortgage conditions allow the receiver to terminate tenancies, along with the power to bring proceedings and seek possession, receivers can also serve notices to terminate existing tenancies such as notices under section 21 Housing Act 1988. The reasoning that receivers may do that which is necessary to achieve the permitted end must therefore extend to other notices such as break notices and other statutory notices which may be required in order to obtain possession.

When seeking to terminate a tenancy under section 21 of the Housing Act 1988, the receiver will need ensure compliance with the requirements in relation to deposit protection, EPC and the provision of information in relation to the tenant's rights. Where there is an uncooperative borrower and tenant, however, it can be quite difficult to obtain the necessary information to ensure compliance. If for example, both the tenant and the borrower fail to provide a tenancy agreement or details in relation to the tenancy, one available option is to treat the occupier as a trespasser and issue a claim on that basis until evidence of any right of occupation is provided. The trespasser route can be used as a tool to flush out whoever is in occupation of the property so that any agreement in place can then be terminated in the correct way.

The agency principle is not always easy for borrowers to get their heads around and quite often even District Judges struggle to distinguish between the borrower and the receivers when proceedings for possession have been brought in the name of the borrower acting by the receiver. This is especially so when the borrower attends court and wants to make submissions. Any borrower who wants to intervene in the receiver's claim for possession against a tenant ought to apply to be joined to the proceedings as a party. However, the reality is that quite often a District Judge will allow them to attend any hearing and voice their opposition without the issue of their standing to participate being formally resolved. This is of course frustrating

for the receiver because it often turns what should be a straightforward claim for possession into a long and drawn out process.

One further area of contention which has not yet been settled by case law is the interaction between a receiver's right to possession and section 36 of the Administration of Justice Act 1970. The section 36 discretion to stay, suspend or postpone possession applies in cases where a mortgagee brings a claim for possession and it appears to the court that sums due under the mortgage could be paid within a reasonable time or any default remedied within a reasonable time. However, if a receiver is appointed over a buy-to-let property, steps can be taken to evict tenants and possession will be acquired without court proceedings brought against the borrower. This acts to bypass the supervisory jurisdiction that the Court would otherwise have had if the lender sought possession directly from the borrower.

In *Ropaigealach v Barclays Bank* [2000] Q.B. 263 the Court considered whether a lender had been entitled to act without a court order in taking possession of the borrower's house and selling it in circumstances where the property stood empty. It was held that section 36 had not abrogated the mortgagee's common law right to take possession of a property where court proceedings are not needed, for example where premises are unoccupied. The higher Courts are yet to consider whether a receiver could do the same. However, it seems to follow from the Court's reasoning that if a mortgagee can in some circumstances take possession without Court proceedings then by extension a receiver can too.

While the relationship between a receiver and lender is certainly a strange one which can result in a number of challenges by borrowers, there are also numerous advantages as highlighted above. The appointment of a receiver and the agency relationship which it creates offers a very practical solution to problems often faced by lenders when they wish to avoid direct liability to the borrower.

Tricia Hemans is a Barrister at Falcon Chambers

Roisin McGlinn is an Associate Solicitor at TLT LLP