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# LPA receivership of buy-to-let properties

## Avoiding pitfalls and managing legal risks





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## LPA receivership of buy-to-let properties Avoiding pitfalls and managing legal risks

Presented by Clive Whitfield-Jones, Partner, Jeffrey Green Russell Solicitors and Associate member of NARA to the CML Arrears and Repossessions Conference, Manchester

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### Important note

**These seminar materials are prepared for illustration purposes only. They do not constitute legal advice and must not be relied on as such. Receivership is a complex and highly technical subject not fully explained in these materials. Readers and seminar attendees should not take any step or make any omission with respect to the subject matter of these seminar materials without taking separate legal advice.**

## The fundamental nature of LPA receivership

1. An LPA receiver is a type of custodian appointed by a mortgage lender under a fixed legal charge with the primary purpose of protecting the mortgage lender, realising the security and repaying the secured debt.
2. LPA receivers are creatures of mortgages. Administrators and trustees in bankruptcy are creatures of statutory insolvency law. Mortgage law and insolvency law are two separate systems.

## The appointment, powers and remuneration of an LPA receiver

3. LPA receivers' basic powers are conferred by s 109 LPA 1925. They are usually referred to as the statutory powers.
4. The statutory powers are very limited, and are totally inadequate for managing, letting and selling BTL property:
  - Power to demand and recover rent and income and give receipts (s 109 (3)).
  - Limited power to insure against fire out of receivership funds when so directed in writing by the mortgage lender (s 109 (7)).
  - Limited power to carry out necessary or proper repairs out of receivership funds when so directed in writing by the mortgage lender (s 109 (8)(iii)).

The following key BTL powers are missing:

- Power to take possession. Thus there is no statutory power to:
  - Dispossess the borrower, tenants or trespassers.
  - Serve s 8 or s 21 notices.
  - Take proceedings for other tenancy breaches.
- Power to sell *backed by a direct power to convey the legal estate*.
- Power to manage.
- Power to borrow.
- Power to let, accept surrenders of tenancies and modify tenancies - unless the mortgage lender delegates to the receivers the exercise of its own circumscribed powers to lease and accept surrenders of leases under LPA ss 99 (19) and 100 (13).

- Power to insure comprehensively.
  - Powers to repair, maintain, alter, improve, decorate and furnish.
  - Power to remove and store possessions, and movable plant and equipment.
  - Power of attorney.
5. Fortunately, many of these powers are often conferred on receivers by the mortgage. These additional powers are called express powers. Please note that express powers are conferred on the receiver by the borrower, not by the mortgage lender. Though the mortgage lender selects and appoints the receiver, the express powers over the mortgaged property are derived from the borrower. This has crucial implications.
  6. If significant additional express property management powers are conferred on the receiver, he or she becomes a receiver and manager, though usually still referred to as a receiver.
  7. Unless the receiver goes to court and persuades the judge to allow higher remuneration (usually an unrealistic option for a high volume BTL receivers) the receivers' remuneration is limited to a maximum of 5% of the gross amount of all monies received in the course of the receivership to include expenses eg. letting agents' fees and repairs. This is a totally unrealistic remuneration and expenses basis for BTL.
  8. Fortunately, many mortgage conditions entitle receivers to remuneration for the performance of their duties and for reimbursement of all costs charges and expenses correctly incurred by them in a manner from time to time agreed in writing between the mortgage lender and the receivers.
  9. Receivers also have implied powers. The grant of an express power implies the grant of implied powers to carry the express power into effect by all lawful means, unless expressly prohibited by the terms of the Mortgage Deed.

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### Discussion Case 1

s 8 and s 21 notices.

Powers of management, sale and letting.

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## Appointment, powers and remuneration - risk management issues

1. A receiver (once satisfied that a particular proposed receivership is appropriate to accept) must take positive steps to ensure that he or she:
  - a. Is validly appointed and actually assumes the powers conferred by statute and by the mortgage;
  - b. Understands over what property he or she is appointed; and
  - c. Understands the nature and extent of his or her duties and obligations as an LPA receiver and the possible serious consequences of failing to perform those duties or exceeding them. There are 3 main dimensions of risk:

### **APPOINTMENT RISK**

### **BREACH OF DUTY RISK**

### **EXCEEDING POWERS RISK**

2. An LPA Receiver should instruct solicitors knowledgeable in receivership law and who hold substantial professional indemnity insurance to carry out all necessary checks and issue a written legal opinion that the appointment is valid. Though this process is usually called “validation” the legal opinion does not validate an otherwise invalid appointment. The “validation” is an opinion, not a guarantee or insurance policy and does not confer complete protection – far from it.
3. A receiver should consider the availability of an indemnity from the appointing mortgage lender.
4. Any indemnity is likely to be limited to the following items as a full indemnity would bypass the partial liability screen conferred on the mortgage lender by the receivership:
  - Invalid or defective appointment;
  - Inability to recover remuneration from receivership assets;
  - Actions directed by or agreed with the mortgage lender.

I accept that in many cases, no appointer’s indemnity will be available.

5. A receiver should take legal advice as to the extent of his or her powers. The underlying principle is that receivers are not omnipotent. They have no powers over a BTL property except powers conferred by statute, powers conferred expressly by the mortgage and associated implied powers. This is an arcane and difficult area of the law and the extent, presence or absence of specific powers can often only be determined with the benefit of expert legal advice.
6. A receiver invalidly appointed (ie. no powers) or validly appointed but exceeding his powers may be held liable in a number of ways including:
  - Trespass;
  - Conversion;
  - Constructive trusteeship;
  - Restitutionary claims for unjust enrichment.

Serious financial consequences may follow.

In *Re Goldberg (No. 2). Ex parte Page*, a business was transferred fraudulently to a company then charged to mortgagees. The mortgagees later appointed a receiver. The transfer was set aside as fraudulent. The charge under which the receiver was appointed fell away.

Held:

- The purported receiver is the agent of his appointor;
- The appointor and the receiver were jointly and severally liable as trespassers; and
- Ordered to pay to the trustee the value of the property (if any) of the bankrupt of which they are in possession, or of which they took possession on or about June 19, 1911, and to deliver up to the trustee all such property of the bankrupt (if any) as remains in their possession or in the possession of either of them.

This is the sort of case where the solicitor issuing the validation opinion would normally be unaware of the background facts, and therefore not negligent in “validating” the opinion.

In *Ford & Carter Ltd v Midland Bank Ltd (1979) 129 NLJ 543 HL* a guarantee was held not to be binding on a company. A receiver appointed under a floating charge supposedly securing the guarantee was held liable as a trespasser.

In *Rolled Steel Products (Holdings) Ltd v British Steel Corporation plc [1986] Ch 246*. The directors of a company acted in breach of the company’s articles of association and their fiduciary duties to the company in purporting to authorise and in executing a guarantee and the debenture.

The defendant corporation and the receiver appointed under the debenture had notice of that breach when they received assets of the Company. They were accountable for those assets to the company as constructive trustees.

7. If a receiver is invalidly appointed, the person responsible for that appointment, ie. the mortgage lender may be vicariously liable for the acts and defaults of the purported receiver.
8. s 34 *Insolvency Act 1986* Liability for invalid appointment.

“Where the appointment of a person as the receiver or manager of a company’s property under powers contained in an instrument is discovered to be invalid (whether by virtue of the invalidity of the instrument or otherwise), the court may order the person by whom or on whose behalf the appointment was made to indemnify the person appointed against any liability which arises solely by reason of the invalidity of the appointment.”

9. If a receiver deliberately misleads a borrower as to the extent of his or her powers the provisions of the Fraud Act 2006 are engaged (see ss 1 to 4).
10. The receiver’s management powers are exercised for the benefit of the mortgage lender not the borrower. The receiver owes no duty in contract or tort to the borrower. The receiver’s duties are traditionally equitable only, basically the same equitable duties owed by the mortgage lender to the borrower and those interested in equity of redemption (eg. subsequent charge holders).
11. TCF does not normally apply to BTL receivership unless the mortgage lender requires the receiver to opt in to TCF or the receiver is acting as agent of the mortgage lender.
12. The mortgage conditions of BTL mortgage lenders are highly variable. There is a broad spectrum. Some mortgage conditions contain no additional receivership provisions at all. Others contain comprehensive powers.

Many mortgage lenders have issued a number of editions of their mortgage conditions. For example, new editions were introduced in 2004 after the introduction of FSMA regulation (even though FSMA regulation does not normally apply to BTL). Receivership powers can vary markedly from one edition to the other. Some mortgage lenders have acquired portfolios of mortgages from other lenders each with several different editions of mortgage conditions.

This means that receivership powers, even for the same appointing mortgage lender, can vary widely from one property to another and receivers must be thoroughly acquainted with their actual powers on a property by property basis. Receivers and mortgage lenders should never assume that comprehensive receivership powers exist, always check. BLT mortgage conditions tend not to include receiver's exclusion or limitation of liability clauses.

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## Discussion Case 2

A BTL unit is in receivership. The loan to the borrower is at 6% fixed for another two years. Arrears are piling up. The exit strategy calls for the property to be held for another year. To reduce accumulating arrears, the mortgage lender wishes the borrower to enter into a "product switch" to a 2% over base tracker mortgage. The borrower cannot easily be contacted because he now lives with his new girlfriend in Panama. Can the receivers sign a product switch form on behalf of the borrower on the basis that:

- The receivers are the agents of the borrower?
- The mortgage conditions contain a power of attorney in favour of the receivers giving them authority:

"to do anything necessary to protect the Lender's interest under this Mortgage...?"

- The receivers are obliged to act in the borrower's best interests in managing the property and a reduced interest rate is in the borrower's interests?

Can the receivers lawfully sign the product switch on behalf of the borrower?

What is the way forward?

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13. What is the position of a mortgage lender when the mortgage deed contains no or inadequate express receivership powers?

- The mortgage lender may appoint a receiver then delegate the exercise of certain of the mortgage lender's own powers to the receiver.
- It may be possible for the mortgage lender to appoint a receiver to carry out a bare LPA receivership (statutory powers only) and for the mortgage lender to enter into a separate property services agreement with a property services company associated with the receiver. Specialist legal advice is necessary, especially as the mortgage lender will wish, if possible, to avoid assuming liability as landlord.

## Capacities in which LPA receiver acts

Broadly, an LPA receiver may act in four main capacities:

1. Agent for the mortgagor.
2. Agent for the mortgagee.
3. As a Principal (ie. agent for no-one).
4. As the attorney of the mortgagor.

It's crucial that for any particular purpose, the receiver understands in which capacity he or she is acting.

## The receiver as agent for the mortgagor (borrower)

Section 109 (2) of the LPA 1925 provides that the LPA receiver..... “shall be deemed to be the agent of the mortgagor; and the mortgagor shall be solely liable for the receiver’s acts or defaults unless the mortgage deed otherwise provides.”

This statutory deemed agency has subtle limitations and the mortgage conditions should (and normally do) expressly constitute the receiver the agent of the borrower.

*See Richards v. Overseers of Kidderminster [1895 R. 1792.]*

At first sight, this is an odd concept. The mortgage lender appoints the receiver to protect the mortgage lender’s interests and the borrower has no control over him or her. So why should the receiver be deemed to be the borrower’s agent and empowered to impose personal liability on the borrower?

The reasons are historic. Mortgage lenders do not normally take possession of mortgaged property unless left with no choice because of the potentially onerous duties to account as mortgagee in possession. If the receiver were the agent of the mortgage lender, the mortgage lender might:

1. Become exposed to liability as mortgagee in possession.
2. Assume liability to tenants as landlord.
3. Assume other potentially onerous liabilities associated with possession of land eg. occupier's liability.
4. Be liable as principal for the wrongdoing, acts and omissions of the receiver eg. property mismanagement, sale at undervalue, breach of contract with an asset manager or managing agent.
5. Be liable for the receiver's remuneration.

My own historical research has revealed that as far back as 1795, borrowers and mortgage lenders agreed, as a matter of contract, that if a receiver were appointed, the receiver would act as the agent of the borrower, shielding the mortgage lender from liability.

Agency in this context is somewhat of a legal fiction. The usual duties of an agent are absent. The supposed principal, the borrower, has no say in the appointment or disappointment of the receiver and cannot give him or her instructions.

The agency of the borrower is in reality a device to protect the mortgage lender, to give the mortgage lender the advantages of possession without its drawbacks. It draws a partial liability screen between the mortgage lender on the one side and the borrower, the property and the tenant on the other.

“Agency” in the receivership context is about who assumes personal liability – the mortgagor, the mortgagee or the receiver.

In *Telsen Electric Co. Ltd v J.J. Eastick & Sons* [1936] 3 All ER 266 the receiver broke a price maintenance contract relating to radio sets, flooding the market with cheap sets. The borrower was held liable for that breach of contract.

Acting as an agent does not absolve a receiver from personal liability for torts eg. trespass or nuisance. “Speaking generally, a person who causes or commits a nuisance does not avoid liability by pleading that he did so as an agent for, or upon the authority of some other person” see Briggs J in *John Smith & Co (Edinburgh) Ltd v Hill and others* [2010] 2 BCLC 556 at para 34.

### **Termination of the receiver’s agency**

A receiver ceases to be the agent of the borrower if that receiver (or one of two joint receivers) receives notice:

- In the case of a borrower who is an individual, when that individual becomes bankrupt, dies or becomes of unsound mind.
- In the case of a borrower who is a company, when that company passes into liquidation.

On termination of the agency, the receiver does not automatically become agent of the mortgage lender and usually becomes a principal ie. not an agent at all. *American Express International Banking Corp v Hurley* [1985] 3 All ER 564.

*Thomas v Todd* [1926] KB 51. The receiver of a company in voluntary liquidation contracted for a band of musicians to play at certain club premises. Held: The receiver was personally liable on the contract. The receiver’s agency had terminated and so he had no authority to bind the company.

If a receiver purports to act as the borrower’s agent when that agency has terminated there is a breach of warranty of authority, and the receiver may be personally liable accordingly. *Lord Herschell in Gosling v Gaskell* [1897] AC 575 at 592.

When a mortgage lender takes possession of a BTL property after the appointment of a receiver, the receiver becomes the agent of the mortgagee.

Though receipt of notice of bankruptcy, death, becoming of unsound mind and liquidation terminate the receiver’s agency, they do not generally terminate the mortgage lender’s or the receiver’s statutory or express powers to manage or dispose of the property.

There are complications with receiver’s powers of disposition (including letting and sale) over a BTL property of a bankrupt borrower who is a sole proprietor, beyond the scope of this seminar.

- *S 306 Insolvency Act 1986.*
- *S 27(1) and (5)(a) Land Registration Act 2002.*
- *S 86 Land Registration Act 2002.*
- *Drew v Nunn [1874-80] All ER Rep 1144.*

A power of attorney granted in favour of a mortgage lender under a legal charge is normally expressed as an irrevocable “security power” and is not revoked by agency termination. A similar power of attorney granted in favour of an LPA receiver is not normally a “security power” (because it does not secure an obligation to the donee (ie. the receiver) and is revocable on the agency termination. This is a pity. The mortgage lender itself will not often require to have recourse to a power of attorney. To an LPA receiver, the power of attorney is a very important tool for executing documents such as contracts, leases, surrenders and land transfer documents.

- *Sowman and others v David Samuel Trust Ltd and another [1978] 1 All ER 616.*
- *Barrows & Others v HM Chief Land Registrar and Another The Times 20 October 1977, 1977 & No 1669, (Transcript: Association).*

## Risk management issues relating to the LPA receiver’s agency

Basic rule: Mortgage lenders do not normally wish the receiver to become their agent because the mortgage lender then becomes liable as principal for the acts and defaults of its agent. The precious list of protections conferred on the mortgage lender by the receiver acting as agent of the borrower will be lost with potentially serious consequences. The receiver may be entitled to an agent’s right to indemnity against his principal.

### I. Dancing too closely to the mortgage lender’s tune.

Where the mortgage lender directs the receiver in the conduct of the receivership, for example by issuing instructions as to how the receiver should act, a court will readily find that the receiver has become the agent of the mortgage lender.

*Standard Chartered Bank Ltd v Walker and another [1982] 3 All ER 938.*

There was evidence that the bank instructed the receiver to realise the company’s assets as soon as possible and that in accordance with those instructions the receiver instructed an auctioneer to hold a sale of the company’s stock very quickly. The guarantors claimed that in consequence of the bank’s instructions the sale was held at the wrong time of the year, that it

was poorly advertised and therefore poorly attended, and that the stock was sold for £42,800 which was considerably less than its real value. The amount realised was barely sufficient to cover the costs of realisation.

Held: There was a triable issue as to whether the bank had interfered, by giving instructions to the receiver, in the conduct of the receivership in respect of the sale of the company's assets, so as to make the receiver its agent.

*American Express International Banking Corp v Hurley [1985] 3 All ER 564.*

There was constant communication between the bank and the receiver and the latter sought the former's approval to such actions as he proposed to take.

Held: Receiver became the agent of the bank and thus liable for the receiver's undervalue sale of sound and lighting equipment used at pop concerts.

## 2. Receiver acting under appointor's instructions.

The mortgage lender may be liable to indemnify the receiver against any liability to the borrower or a third party incurred by the receiver whilst acting under the instructions of the mortgage lender.

*In re B. Johnson & Co. (Builders) LD. [Manchester, 1948 B. No. 2. Liverpool, 1948 B. No. 5710.]*

## 3. Landlord liability, authorised and unauthorised tenancies, tenancy by estoppel.

Consider the package of liabilities and obligations that goes with being a BTL landlord under short term ASTs:

- a. the burden of the landlord's express covenants contained in the AST.
- b. the burden of landlord's covenants implied in the AST by statute and in particular under section 11 of the Landlord and Tenant Act 1985 which imposes obligations on the landlord to repair the structure and exterior (including drains, gutters and external pipes) of the premises; to keep in repair and proper working order the installations in the premises for supply of water, gas and electricity and for sanitation (including basins, sinks, baths and sanitary conveniences, but not other fixtures, fittings and appliances for making use of water, gas or electricity); to keep in repair and proper working order the installations in the premises for space heating and heating water.

- c. the burden of other obligations imposed by statute for example under the Gas Safety (Installation and Use) Regulations 1998, the Electrical Equipment (Safety) Regulations 1994 and the Plugs and Sockets etc., (Safety) Regulations 1994 and the tenancy deposit scheme.

The law recognises two basic types of possession of land, physical possession and possession of rents and income. A mortgagee is entitled to possession. Thus, a mortgage lender need not appoint a receiver in order to intercept rents. A mortgage lender could simply write to the tenants directing them to pay rents to the mortgage lender. Mortgage lenders do not do this as they would become landlord and assume landlord liability.

A receiver acting as agent for the borrower may safely accept rents without either that receiver or the appointing mortgagee assuming landlord liability.

If a receiver acting as agent for the mortgage lender accept rents that is the same thing as the mortgage lender itself accepting them, with the potential for assuming landlord liability.

It is particularly dangerous for the mortgage lender where the tenancy is unauthorised and on onerous terms eg. a 5 year tenancy at a fixed low rent. A receiver may well be able to accept rent under an unauthorised tenancy without prejudice to the mortgage lender's right to obtain possession against the tenant as a trespasser. If the receiver is acting as agent for the mortgage lender, the mortgage lender may find itself bound by that tenancy and unable to remove the tenant. The security may be difficult to realise and its value greatly impaired.

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### Discussion Case 3

Does a receiver become the landlord of property in receivership?

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### Discussion Case 4

Chatsworth Properties Ltd v Effiom [1971] 1 All ER 604, [1971] 1 WLR 144 CA.

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The mortgage lender's solicitors wrote to unauthorised tenant informing him that the mortgage lender had appointed R as receiver of the rents and profits of the property, and continued: 'Please take notice that henceforth you should not pay any sums to your former landlords the mortgagors] but to [R] ...' The mortgage lender appealed from an order refusing their claim for possession: Held: the receipt of rent by a receiver appointed by a mortgagee did not, without more, create a tenancy by estoppel as against mortgagee; but..... What?

## Indemnity insurance issues

1. A receiver should, so far as is possible, obtain indemnity insurance against the risks inherent in receivership activities.
2. “Employed receivers” should consider the following points:
  - Check the employer’s receivership indemnity policy. This policy may cover a multitude of risks arising in other parts of the business. Is the amount of cover adequate? Might cover be exhausted by other claims? What is the excess per claim? Can the receivers’ interest be noted on the policy? Can specific ring-fenced cover for the receivers be obtained? Will the employer be around for many years to come? Insurance is likely to be available on a claims made basis. Will an adequate policy be in effect many years from now when claims might be made? Is run-off cover available?
  - Is an express employer’s indemnity available? Any implied employee’s indemnity may prove inadequate.

## Some landlord and tenant issues

LTA 1987 s 47

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### 47 Landlord’s name and address to be contained in demands for rent etc

- Written demands for rent and other sums payable under a BTL tenancy must contain the name and address of the landlord.
- Where the landlord’s address is outside England and Wales, an address in England and Wales must be given at which the tenant can serve notices and proceedings on the landlord.
- Failure to comply – service charge and administration charge elements of demand are irrecoverable whilst default subsists.
- The borrower is usually (but not always) the landlord.

## LTA 1987 s 48

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### 48 Notification by landlord of address for service of notices

- A landlord under a BTL tenancy must give the tenant an address in England and Wales at which notices (including notices in proceedings) may be served on the landlord by the tenant.
- Failure to comply – rent, service charge and administration charge elements of demand are irrecoverable whilst default subsists.
- The borrower is usually (but not always) the landlord.

### Risk management issues

1. Does the tenancy agreement or ancillary documentation comply, if not serve notice.
2. Consider giving receiver's address as agent for landlord.

## LTA 1987 s 50

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### 50 Continuation of former landlord's liability to tenant where no notice of assignment

Where the reversion to a BTL tenancy is assigned the old landlord remains liable any breach of any covenant, condition or agreement under the tenancy until the tenant is given notice in writing of new landlord's name and address.

### Risk management issues

Should a receiver selling under an express power of sale give notice to the tenant to protect the borrower landlord?

## The unfair relationship provisions in sections 140A and 140B of the Consumer Credit Act 1974

- A lender's buy to let book is normally understood to consist of agreements which are not regulated consumer credit agreements, either because they exceeded the financial limit that applied at the date when they were made (£25,000 up until 6th April 2008) or because they fall within the exemption provided by section 16C of the Consumer Credit Act 1974 (since 31 October 2008) or the one provided by the Consumer Credit Act 2006 (Commencement No.4 and Transitional Provisions Order) 2008 (6th April 2008 to 31 October 2008).
- The unfair relationship provisions in sections 140A and 140B of the Consumer Credit Act 1974 (which were introduced by the 2006 Act) do apply to such buy to let agreements.
- Therefore, if there was to be anything about the terms relating to the appointment of the receiver, or the way in which the lender exercised its right to appoint a receiver, or the way in which the lender directed the receiver to act, which resulted in the relationship between the lender and the borrower being unfair to the debtor, the borrower could apply to the court to have that unfairness rectified by an order under section 140B.

## Consumer Credit Act sections 16C(5) and 126

Appears to prevent the appointment of a receiver without an order of the Court where security was agreed to be given over a BTL property and the agreement was made on or after 31 October 2008 as appointment of a receiver is enforcement of security.

**Thanks for listening**



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