

Research Article

The Legal Threshold of Rights and Liabilities of the Mortgagor, Mortgagee, and Lessee of a Mortgage Property in Relation to the Validity of a Lease

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Abstract

The general position of the law is that, subject to the agreement of the parties to a mortgage transaction, both the mortgagor and mortgagee of a leased property have power to lease mortgaged property. The only condition that needs to be satisfied is that the party leasing must be in possession. While the rights and liabilities of the mortgagor and mortgagee in relation to the mortgage contract poses no problems, the various legislations on mortgage do not provide for the rights and liabilities of a lessee where the property, subject matter of a mortgage, is leased. It would seem that the lessee is subject to the terms of the contract between the mortgagor and mortgagee which he is not privy to. This situation may pose more challenges than is evident and recourse would be had frequently to equity. A threshold implies a boundary of a right. In the realm of property law, the Mortgagor, Mortgagee, Lessor, and Lessee have a multitude of individual rights. However, when these parties interact, not all of these rights are accommodated. Some are modified, and others are limited. The writer, in this paper, intends to conceptualize the interaction of leases in a mortgage transaction. The major jurisdiction explored is Nigeria, with a glimpse on how other jurisdictions comparatively handle similar transactions. This paper seeks to examine the limit of the rights and liabilities of a mortgagor, the mortgagee and lessee in relation to each other in the event of a valid lease of property subject to a mortgage with a view to proposing reforms in this important area of the law and property transaction.

Keywords

Mortgage Property, Lease, Rights and Liabilities, Threshold, Mortgagee, Lessor, Mortgagor, Lessee

1. Introduction

The right to create a lease is usually that of the lessor which is, in the context of this discourse, the mortgagor of a mortgaged property. This right is exercisable both before and after a mortgage transaction is made. A mortgagee can also create leases over a mortgaged property, only after the mortgage transaction has formally constituted. In every mortgage

transaction, especially a legal mortgage, the incidents of the mortgage transaction is clearly delineated in a mortgage deed. Both the mortgagor and mortgagee are bound by covenants which authorize either party to carry out or refrain from carrying out certain tasks. Usually, there would be a covenant on lease/sublease of a mortgaged property. The covenant

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may either permit the mortgagor or mortgagee, as the case may be, to lease the property (either absolutely or subject to certain terms and conditions) or prohibit creation of leases on the property.

The incidents of the relationship between these parties whether the lease is created prior to the mortgage transaction or subsequent to it is the focus of this paper.

2. The Nature of a Mortgage

A mortgage is a conveyance of land or an assignment of chattels as security for the payment for a debt or the discharge of some other obligations for which it is given, subject to a condition that the title shall be reconveyed if the mortgage debt is liquidated. [1] Also, mortgage is a financial arrangement between two parties where the lender gives money in return for the right to take/own a property when there is a default in repayment of the principal sum or any accrued interest. Simply put, a mortgage is a loan secured by a real estate/property. It involves a series of regular payments divided into principal and interest, over a specified period of time. [2] This agreement is secured by the property which serves as a collateral. [3] Another instance of a mortgage transaction occurs in the purchasing or maintenance of a home, land, or other types of real estate. This involves a loan from a bank or mortgage institution which is used by the borrower to purchase a home. The collateral for the mortgage is the home itself. The effect is that if the borrower does not maintain consistent and regular payments to the lender and defaults on the loan, the lender can sell the home and recoup its money. [4] A mortgage is considered a very safe form of loan with minimal risk as the lender can always fall back on the property (which is usually of higher value than the loan sum) if there is a default. [5]

The features necessary to constitute a mortgage were stated in *Waldron v Bird*¹ as follows:

- 1) There must be a promise by the alleged mortgagor to repay money to the alleged mortgagee or to perform some other obligation;
- 2) As security for repayment of such moneys or performance of such obligation, the alleged mortgagor must transfer or assign his estate and interest in property, real or personal, to the mortgagee absolutely;
- 3) To distinguish between an absolute transfer of title and a mortgage, the transfer or assignment must, in order to constitute a mortgage, be subject to a proviso that if and when the mortgagor makes repayment or performs the obligation imposed upon him, the mortgagee will re-transfer or reassign the property to the alleged mortgagor.

This third feature emphasises the age-old principle that prevents a clog on the equity of redemption: "Once a mortgage, always a mortgage." This principle which is the crux of

all mortgage transactions means that a borrower cannot contract to give up his automatic right to redeem title to his property once the debt is paid².

2.1. Who Are the Parties in a Mortgage Transaction

Generally, a mortgage takes the form of a dual mortgage and has just two parties- the mortgagor (being the borrower), and the mortgagee (being the lender). However, there are instances of a tripartite mortgage. A tripartite mortgage like the name implies involves three parties. In many jurisdictions, this form of mortgage is utilized during construction of houses to secure a bridge loan; where the third party is the builder; while the other parties are the lender and the borrower (buyer of the house/future home owner). Usually, the loan is for a property that is yet to be built. The arrangement is that the buyer obtains a loan from the financial institution to purchase a property which is still under construction. [6] Each party enjoys rights over the property. The builder gets a construction lien over the property in the event that he completes the work without getting full payment, while the lender has the usual rights of a mortgagee as will be explored below. Another characteristic the tripartite mortgage of such sort has is Subrogation. Subrogation is a legal process which determines who, how, and when various securities in the property are transferred between the parties. For instance, in the event of the death of the borrower, the builder may retain the first right to claim what the builder is owed for time and materials; also, the bank would then retain the lien on the remaining assets (that is, the land itself).

Another situation that seemingly creates a tripartite mortgage is what is technically referred to as a "guarantor mortgage". A guarantor mortgage is created in situations where they have no credit history (or bad credit history) with the lender, or; they lack the required cash deposit in the lending bank, or; they have no property valuable enough to secure the loan, or; the borrower is a minor. The guarantor, which is often a close family relative or a parent, acts as a guarantor to the loan transaction by using either their savings with the mortgage institution or their property as a security for the loan. [7] The financial risk is that where the borrower defaults, the guarantor has the legal responsibility to repay the loan. Consequently, lenders request for persons above the age of 21, who are financially stable or own a property themselves. [8]

On the other hand, there are qualifications usually required of the mortgagee in a mortgage transaction. It should be noted that the requirements would depend on the quantum of the principal sum being advanced and also the project the principal will be applied to. Among others, these qualifications include:- [9]

1 [1974] VR 49

2 This was first enunciated in the English case of *Vernon v Bethell* (1762) 28 ER 838.

- 1) Age requirement Income requirement³
- 2) Credit history⁴
- 3) Down payment
- 4) Insurance of the property intended to be the collateral
- 5) Legal documents.

2.2. Types and Modes of Creation of Mortgages

Mortgages are of two types, legal and equitable. Legal mortgage is one created pursuant to relevant statutory provisions and is usually made by deed. Equitable mortgage, on the other hand, is one that needs not comply with the full provisions of the relevant statutes governing the transaction and is governed by the rules of equity. It is usually not made by deed and merely confers equitable title on the mortgagee.

There are different forms of creation of a mortgage depending on the location of the property and the nature of the mortgage transaction. An equitable mortgage is usually created through one of the following means:

- 1) Deposit of title deeds
- 2) Agreement to create a legal mortgage
- 3) Equitable charge
- 4) Imperfect legal mortgage⁵
- 5) Assignment of equitable interest in property

As expressed earlier, legal mortgage is governed by relevant statutes. In Nigeria, due to the plurality of the legal system, different laws govern the creation of legal mortgage and a primary consideration for determining the applicable law is the location of the property. A legal mortgage is created through any of the following means:

- 1) Assignment of the mortgagor's unexpired interest in the land with a covenant for re-assignment on redemption of the mortgage.
- 2) Sub-demise⁶
- 3) Demise⁷
- 4) Charge by deed expressed to be by way of legal mortgage
- 5) Charge by deed expressed to be by way of statutory mortgage

Regardless of the mode of creation of a legal mortgage, the incidents are the same in terms of covenants – rights of mortgagee in the event of default.

3. How Can a Mortgage Be Created

The pattern adopted to create a mortgage usually depends on the type of the mortgage. Using Nigeria as a case study, there are just two types of mortgage- the Equitable mortgage and the Legal mortgage. In this context, an equitable mort-

gage involves the transfer of the mortgagor's beneficial interest in an asset to the mortgagee by way of security for the loan sum or the performance of obligations on the condition that upon fulfillment of the obligations, the beneficial interest will be retransferred. The distinctiveness of an equitable mortgage is that the formalities to create a legal mortgage have not been completed or the property being mortgaged is only an equitable interest. Since it is only the beneficial interest in an asset transferred, an equitable (rather than a legal) mortgage is created. On the other hand, a legal mortgage transfers the legal interest (that is, the outright ownership in the land) to the mortgagee as security for the loan sum/for the performance of obligations. [10]

Furthermore, the creation of either of the types of mortgages in Nigeria is jurisdiction dependent. When creating the equitable mortgage in the Old Western region, or the Eastern, and Northern states in Nigeria, the methods which may be adopted, according to O. Seun-Oguntuga⁸, are:

- 1) Deposit of title deed with the intention to create a mortgage or accompanied by Memorandum of Deposit evidencing the transaction
- 2) Agreement to create a legal mortgage.
- 3) Equitable charge on the mortgagor's property
- 4) Mortgage of an equitable interest e.g mortgage of a beneficiary's rights under a trust.
- 5) An inchoate legal mortgage

In Lagos State, Nigeria, the mode of creating equitable mortgage is slightly different. The Mortgage and Property Law [MPL] of Lagos, 2012, provides in Section 18 that a mere deposit of title deeds or charge on a property is insufficient in creating an equitable mortgage of a right of occupancy. It mandates that such deposit must be accompanied by an agreement to create a legal mortgage in favour of the mortgagee. Otherwise, if the mortgage is to be created over an equitable interest in a property, it has to be by an assignment of an equitable interest in favour of the mortgagee with the provision for cesser on redemption. This law also creates a level of protection for the mortgagee by giving him a leverage to institute an action in court to mandate the mortgagor to execute a legal mortgage in his favour if such is not done within 30 days of the agreement. This additional provision in Lagos State, bequeaths an equitable mortgagee with similar powers of a legal mortgagee.

On the other hand, the creation of a legal mortgage is statutorily provided for in the various Land laws of states. The Conveyancing Act [CA] 1881 (applicable to the Northern and Eastern Nigeria) permits three (3) ways a legal mortgage may be created. These include by an assignment of the legal interest in the property; or by a sub-demise of a portion of the residue interest; or by a statutory mortgage. It is noteworthy that under the Property and Conveyancing Law [PCL] of 1959 applicable to the old Western region of Nigeria, in as much as it recognizes the demise of the entire interest (with a

³Above infancy, minimum age of 21 years.

⁴ A consistent and steady source of income, sufficient evidence including but not limited to 'bank account statements or pay slip'

⁵ Walsh v Longsdale [1882] 21 Ch. D 9.

⁶ Leasehold estates only

⁷ Freehold estates only

⁸Taking security: A Review of Mortgage Creation under Nigerian Law, Nigeria (2020, June 15).

cesser for redemption) as security, this was only applicable to a freehold interest⁹. The later enacted Land Use Act of 1978 transforms all previous freehold interests into leasehold through the radical vesting of title on all lands in the Governor of the State¹⁰.

Consequently, a legal mortgage in the West (inclusive of Delta State and Edo State)¹¹, is limited to sub-demise for a term of years absolute, less one day at least than the term of years vested in the mortgagor and subject to a provision for cesser on redemption; or a charge by deed expressed to be by way of a legal mortgage; or by statutory mortgage. In Lagos, the Mortgages and Property Law 2012 provides for Demise for a term of years absolute subject to a provision for cesser on redemption; Charge by deed expressed to be by way of statutory mortgage; Sub-demise for a term of years absolute, less by one day at least than the term of years vested in the mortgagor and subject to a provision for cesser on redemption; and Charge by deed expressed to be by way of legal charge¹². It is arguable that the recognition of demise despite the imposition of the Land Use Act is because the Land Laws of Lagos State recognize that those who had freehold prior to the Land Use Act now have "Deemed grants".

The focus of this article is not just to consider in generality the concept of a mortgage, but to explore the concept of leases in an existing mortgage. A lease is differentiated from a mortgage in the sense that, a lease is the conveyance of the possession of a land/property to another for a specific period of time in return for a periodic payment. Unlike a mortgage where the interest in the property is being given as a security for a debt, the intention of a lessor is not to transfer the interest in the property as security, but rather, a right to use the property in exchange for a consideration called "Rent". The lessee does not become the owner of the property by reason of the rent paid. Another difference between a lease and a mortgage is that the lessor must part with possession of the property in consideration for the rent while the mortgagor can retain possession during the period of the mortgage.

4. Leases in Mortgages

Leases can exist in the realm of mortgages. On the part of the mortgagee, it exists when he is in possession¹³. While, on the part of the mortgagor, it is through the right called "Equity of Redemption". Equity of redemption is the equitable interest which a mortgagor has in the land as the owner. It arises in favour of the mortgagor as soon as the mortgage is created and continues until the property is sold or foreclosure occurs. It is the invisible label equity places over the property that treats the mortgagor as continuing to be the owner of the property, subject only to the mortgagee's interest which is

not a right to the mortgaged property but to the mortgage debt. [11] By virtue of this right, the mortgagor can lease out the same property which is subject to the mortgage to a third party. An understanding to this can be gleaned from the words of Lord Selborne in *Heath v. Pugh*¹⁴:

The true nature and character of a mortgage (should be) borne in mind: It is a mere security for the debt, and (subject to the paramount liability of this debt) the mortgagor retains an estate which can be granted and demised.

In like manner, there is a possibility of mortgaging a property which is subject to an existing lease. In such an instance the principle of *qui prior est tempore potior est jure* (where the equities are equal, the first in time prevails) applies. Consequently, the mortgagee and any purchaser of the said property will be bound by the lease and his rights will be subject to the lessee's rights. This was graphically seen in *Gomez v. Williams*¹⁵. In that case, the defendant/lessee was a yearly tenant when the landlord mortgaged the property. The mortgagee sold the property to the plaintiff when the landlord defaulted. Thereafter, the plaintiff wrote to the defendant that his tenancy had been converted to a monthly tenancy. On failure of the defendant to comply, the plaintiff sued the defendant claiming arrears of rent, mesne profits, and recovery of possession. The court ruled against the plaintiff on the reason that the purchaser cannot have a better title than the vendor. Consequently, if the vendor sells a property already in occupation of another under a tenancy agreement, the purchaser buys subject to that tenancy. The purchaser takes over the property on the terms of the tenancy and the nature of that tenancy can be varied by the purchaser only with the consent of the tenant.

4.1. Subsequent Leases: The Rights and Liabilities of the Mortgagee, the Mortgagor, and the Lessee

As a matter of fact, the Conveyancing Act, Property and Conveyancing Law, and the Mortgages and Property Law of Lagos State recognize leases subsequent to a mortgage provided no contrary intention is expressed in a Mortgage deed. Such leases operate subject to the terms of the mortgage deed¹⁶. The relationship among the mortgagor, mortgagee and lessee would be considered under the scenarios below.

SCENARIO 1

Where the lease is created before the property is mortgaged by the mortgagor, the validity of the lease will be decided in accordance with the elements listed above. The lease, if valid, is binding on the mortgagee. There are two schools of thought on whether the lessor/mortgagor would still be entitled to collect rents. The first school is of the view that the right to collect rents vests in the mortgagor and not the

9 s. 108 PCL 1959

10 s. 1 of the Act

11 ss. 109 & 110 of PCL 1959

12 ss. 15 & 16 MPL

13 s. 121(2) PCL

14 [1881] 6 QBD 345; 359

15 [1972] NMLR 149, per Taylor CJ

16 s. 18 (13) CA; s. 121 (12) PCL; s. 33(12) MPL., Lagos.

mortgagee. [12] The second school of thought is of the opinion that in the case of a lease created before the mortgage of the property in issue, there is privity of estate between the mortgagee and the lessee. [13] This seems to suggest that the right to collect rent would vest in the mortgagee upon the execution of the mortgage deed.

In the first instance, only where there is default in repaying back the mortgage sum and/or interest and a receiver is appointed in accordance with the mortgage deed does the mortgagee have the right to rents on the property. This is however, not an indefinite right and he stops receiving rent as soon as the mortgage sum/and or interest is satisfied.

In all cases, the right of the lessee in relation to exclusive possession, enjoyment of the premises, non-derogation of grant and insurance (where the duty to insure is on the lessor) are not detracted from. In addition, the obligations of the lessee are intact. The only qualification arises with respect to payment of rent. At all times, the obligation to pay rent exists with the exception that where a receiver is validly appointed over the property, the lessee must pay the rent to the receiver who determines how the money should be applied in satisfaction of the mortgage sum and/or interest.

Where, however, the mortgagee chooses to exercise his power of sale under the mortgage deed while the lease subsists? Two options appears to be available to him viz:

- 1) He would be allowed to do so. His interest in the property is legal while that of the lessor is equitable and legal interest prevails over equitable interest. The lessee must, however, be adequately compensated for his loss of equity. The party to compensate would depend on who has been habitually collecting rents during the subsistence of the mortgage.
- 2) His right to sell would be suspended to cater for the equitable interest of the lessee especially where the lease is about to expire.

SCENARIO 2

Where a property which is the subject of a mortgage is subsequently leased to a third party, the lease must contain the valid elements of a lease to be valid. It must also be created in accordance with the covenant on lease in the mortgage deed or statutory provision where such covenant is absent. Usually, the lease would be stated to be created subject to the covenant in the mortgage deed. In order to avoid technicalities and complexity, it is appropriate that the term of years granted under the lease should be shorter than the period within which the mortgage debt must be satisfied.

Certain agitations may bother ones mind in the course of these situations.

Where the lease is created by the mortgagor, could there be privity of estate between the lessee and the mortgagee and vice versa?

Who is entitled to rent? Is it the party that created the lease?

In the event of default where the lease is created by the mortgagor, what is the position of the lessee?

Where the mortgagee leases and the mortgagor discharges the mortgage, does the lessee then pay the mortgagor the rent? It is submitted that in this case, the principle of novation will apply. Novation is 'the act of substituting for an old obligation with a new obligation or replaces an original party with a new party'¹⁷.

SCENARIO 3

A lease created in breach of covenants in the mortgage deed (particularly the covenant with respect to lease/sublease of mortgaged property) is a lease in estoppel. A lease in estoppel is legally binding on both parties to the lease. It is also binding on the other party to the mortgage transaction. In *Church of England Building Society v Piskor*¹⁸, a mortgagee was held to be bound by the lease agreement between the mortgagor and lessee.

It shall further be explored here, the extent of rights the mortgagor, mortgagee and lessee have in creation of subsequent leases.

4.2. The Mortgagor

The Right to Lease: As previously mentioned, the statutes¹⁹ now enable the mortgagor to lease the mortgaged property provided that the mortgagee is not in possession. The Conveyancing Act 1881 expanded the power of the mortgagor in this particular by allowing him to grant leases for limited periods that would be binding upon the mortgagee. The present position is governed by the Law of Property Act 1925, which confers upon a mortgagor in possession a statutory right to grant Agricultural or Occupational Leases, as well as Building Leases, the Property and Conveyancing Law 1959 as well as the Mortgages and Property Law of Lagos State 2012 provide for only building leases²⁰. Some authors, such as the learned writer [E. Chianu, 2017], have argued that the courts will give a broad interpretation to the kind of leases which the mortgagee can grant vis-à-vis the binding nature of the lease on the mortgagee given the definition in the Recovery of Premises Law, and the Rent Control and Recovery of Residential Premises Law. Other limitations the statutes impose on this right is that the lease must not exceed Ninety-nine (99) years and the lessee must take possession within twelve (12) months of the grant and must erect the building within five (5) years of the grant. Additionally, the statutes bar the mortgagor from collecting rent in advance in such cases. This provision is to protect the lessee in instances where the mortgagee decides to take possession before the expiration of the term of lease. It need to be mentioned as well that, at common law a mortgagor is entitled to grant a lease binding between him and the lessee, and his power in this respect has not been affected by statute but must be granted with the concurrence of the mortgagee, oth-

¹⁷ Bryan Garner, Black's Law Dictionary, 9th Edition, page 46

¹⁸ [1954] Ch 553

¹⁹ *ibid*, n16

²⁰ see particularly s. 33 MPL, see also Law of Property Act 1925, s.99(1) (3) and *Rust v Goodale* [1957] Ch 33, 39.

erwise it confers only a precarious title upon the lessee²¹. The paramount title of the mortgagee may be asserted against both him and the mortgagor. [14]

Right to Collect Rents: Except in instances where the mortgagee has taken possession of the property, the mortgagor has the right to collect the rents from the tenant/lessee and has no liability to account to the mortgagee. In *Gory v. Nomuoja*²², Ovie-Whiskey J opined:

I cannot see how a mortgagor in possession of his landed property can render accounts to a mortgagee for the rents collected from the property by the mortgagor. In the eyes of equity the mortgagor remains the true beneficial owner of the property notwithstanding his grant of a term of years absolute to the mortgagee and as long as he remains in possession he is entitled to appropriate the rents and profits to his own use without any liability to account for them, even though he may be in default in the payment of interest²³.

A Right to Redeem the Property (entailing both the legal right and equitable right to redeem): the right to redeem is what distinguishes a mortgage from a sale. The renowned phrase “once a mortgage, always a mortgage” as firstly espoused in the case of *Harris v. Harris*²⁴, is a depiction of this most important right which a mortgagor enjoys. The intent of this right is that a mortgage cannot be made irredeemable and a provision to such effect is void. It also bars the mortgagee from reserving to himself any collateral advantage outside the mortgage agreement. This right creates a protection for the mortgagor to the effect that time is not a negative essence in the transaction. Consequently, the mortgagor has the right to pay back the mortgagee the principal sum, including the interest, and redeem his property at any time until it is appropriately and effectively extinguished either by the acts of the parties concerned or by a proper decree of the competent court. [15] The legal right to redeem is the timeline agreed upon expressly by the parties. It is referred to as the “legal due date” for the payment of the mortgage sum. This date does not prevent the mortgagor from redeeming earlier, but it only marks a time at which certain rights of the mortgagee such as right of sale arises. However, when this legal right expires, the equitable right to redeem begins. The equitable right to redeem should not be misconstrued for the equity of redemption. While the former is an extended hand of grace by equity, the latter refers to the compendium of interest a mortgagor retains in the property after conveying the legal estate to the mortgagee.

Regardless of an existing lease on the premises, the mortgagor upon full payment of the principal sum and interest accrued has a right to redeem the property. As mentioned

above, if the mortgagee had taken possession and received rents, he shall account to the mortgagor as well as transfer the balance left to the mortgagor.

Right of Action to Recover Possession: Section 120 of the PCL empowers the mortgagor to sue for the possession, recover rents or profit, prevent or recover damages in respect of a trespass or other related wrong, in his name provided the mortgagee has not given notice to take possession. Notably, if the lease agreement contains a reentry/forfeiture clause in the event of rent being held in arrears, the mortgagor/lessor has a right to recover possession upon a breach by the lessee. But in instances where the aforementioned clause is absent, the mortgagor/lessor may recover damages from the lessee²⁵. Interestingly, the statutes in Nigeria mandate the inclusion of a re-entry clause in the lease agreements. But such re-entry will occur when the rent has not been paid within a time specified, not exceeding 30 days²⁶.

Right to Accept Surrender of Leases: The PCL and the MPL further recognize the right of the mortgagor to accept the surrender of any lease of the mortgaged land or any part of it comprised in the lease while in possession. Where any consideration for the surrender other than an agreement to accept an authorized lease is given by or on behalf of the lessee to the mortgagor, the acceptance is subject to the consent of the incumbrancers or prior incumbrancer in a case of a subsequent surrender²⁷. If only a part of the leased land is surrendered, the original lease may be varied in a manner the mortgagor is authorized to so grant. Furthermore, on a surrender and making of a new or other lease, whether subject or not to the same or other covenants, provisions, or conditions, the value of the lessee's interest in the lease surrendered may be taken into account in the determination of the amount of the rent to be reserved and of the nature of the covenants, provisions and conditions to be inserted in the new or other lease.

4.3. The Mortgagee

The Right to Lease: Given that the legal estate in the property is transferred to the mortgagee, the mortgagee has the capacity to lease the property. However, the prerequisite for this is that the mortgagee has to come into possession first²⁸. The kind of lease that can be granted is similar to that of the lease by the mortgagor. Furthermore, all other statutory guidelines applicable to a lease by a mortgagor also applies to a lease by a mortgagee.

Right to Refute a Lease: Under the Common law, a legal mortgagee is not bound by a lease created by the mortgagor after the mortgage, except such is made with the concurrence of the mortgagee. [16] This rule was based on the principle of priorities. Consequently, this entitled the mortgagee to

21 s.121(13) and s.122 PCL; Law of Property Act 1925, s.99(14); *Iron Trades Employers Insurance Associations Ltd v Union Land and House Investors Ltd* [1937] Ch 313.

22 [1969] Nig Comm LR 25

23 see also *Gomez v. Williams* (1972) NMLR 149.

24 [1681] 1 Vern 33

25 *Whail v Bunman* [1953] 2 QB 198.

26 s. 18(7) CA; s. 121 (13) PCL; s. 33(6) MPL.

27 s.34 MPL; s.122 MPL

28 s. 18(2) CA; s. 121(2) PCL; s. 33(2) MPL.

treat the lessee as a trespasser, evict such tenant/lessee and recover possession. This right can however only apply when the mortgagee has not done any act that confirms the lease. Such act includes acquiescence after coming to the knowledge of the lease. Farwell J, in *Iron Trades Employers Insurance Association v. Union Land & House Investors*²⁹, states:

The mortgagee as soon as he ascertained that the mortgagor had granted a lease to a third party was entitled to take steps immediately to evict the tenant, to treat him as a trespasser and subject to the tenant's right to redeem, the mortgagee could evict him and recover possession of the property. On the other hand, he might if he desired, confirm what had been done, but if knowing the facts, he stayed his hands and did nothing, he might find himself in danger of being held to have acquiesced in and thereby confirmed the lease and therefore not entitled to oust the tenant.

Worthy of note here is that there has been a statutory modification of this common law position by virtue of Section 121 of the Property and Conveyancing Law 1959, Section 18 of the Conveyancing Act 1881, and Section 33 of the Mortgages and Property Law of Lagos State 2012 which permit a mortgagor to grant a building lease. Consequently, where a mortgagor complies with the statutory provisions, the mortgagee cannot rely on the Common law to refute the tenancy/lease created. However, the mortgagee can exclude this statutory enablement in the mortgage instrument by expressly prohibiting the mortgagor from leasing out the property during the mortgage.

Right to Take Possession: Generally, a mortgagee by reason of obtaining the legal estate being transferred to him has a right to take possession of the mortgaged property. In *Four Maids Ltd v. Dudley Marshall (Properties) Ltd*³⁰ Harman J., stated:

The right of the mortgagee to possession in the absence of some contract has nothing to do with default on the part of the mortgagor. The mortgagee may go into possession before the ink is dry on the mortgage unless there is something in the contract, express, or by implication, whereby he has contracted himself out of that right. He has the right because he has a legal term of years in the property or its statutory equivalent.

Flowing from the above, the mortgagee can take possession to the end of evicting the lessee or demanding rents. In *Corbett v. Plowden*³¹, the court noted that, although a lease is good between the lessee and the mortgagor who granted it, the paramount title of the mortgagee may be asserted against the both of them. Also, in *Britannia Building Society v. Earl*³², the mortgage deed had prohibited the mortgagor from granting leases in the course of the mortgage. However, the mort-

gagor breached this covenant and let out the property. When the mortgagor fell in default, the mortgagee sought possession against the lessee and the mortgagor. The court granted the application of the mortgagee noting that the tenant only had a right against his landlord and not the mortgagee.

Right to Collect Rents: This right flows directly from the preceding right to take possession. The mortgagee may take possession either in person or by means of an appointed receiver. Once the mortgagee comes into possession, he becomes entitled to all arrears of rent that the lessee owes (including all accrued at the time the mortgagee takes possession and after). Notably, the rents do not extend to those accrued before the existence of the mortgage. The entitlement does not operate automatically. As a perquisite, the mortgagee must give the tenant a notice of the mortgage (that is his legal estate in the property) as well as a notice of his intention to take possession and also a formal demand of the rent³³. Furthermore, an exercise of this right incurs a liability to give account. The court held in *White v. City of London Brewery*³⁴, that this liability extends to sums the mortgagor ought to have received but for a default on the part of the mortgagee. In addition to giving account, the mortgagee must ensure that the rent reserved is the best obtainable for the property.

Another dissatisfactory liability of the mortgagee collecting rents is that it subjects the mortgagee to collect his principal sum in trickles. This is because the rent received will be first applied in the payment of rates and repairs, and secondly applied in the satisfaction of the principal sum. Also, once the debt is fully liquidated, and possession is returned to the mortgagor, the mortgagee is mandated to return the balance of the rent paid to the mortgagor. [17]

Right to Accept Surrenders: Similar to the right of the mortgagor, the mortgagee, so long as he is in possession, against all prior or other incumbrancers, if any and also against the mortgagor has power to accept surrenders of lease. If only a part of the leased land is surrendered, the original lease may be varied in a manner the mortgagor is authorized to so grant. Furthermore, on a surrender and making of a new or other lease, whether subject or not to the same or other covenants, provisions, or conditions, the value of the lessee's interest in the lease surrendered may be taken into account in the determination of the amount of the rent to be reserved and of the nature of the covenants, provisions and conditions to be inserted in the new or other lease. [18]

4.4. The Lessee

The position of the lessee is the most delicate. The lessee is like the proverbial grass that suffers during the fight of two elephants. The reason being that, his rights and liabilities are dependent on both the mortgagor and mortgagee. During the period of the mortgage, his rights are distilled, in the sense

29 [1937] 1 Ch. D 318-319.

30 [1957] Ch 317

31 1884] 25 Ch D 678

32 [1990] 2 ALL ER 469

33 see *Turner v Walsh* [1909] 2 KB 484

34 (1889) 42 Ch D 237

that the person to whom he is obligated is usually apparent by the party in possession of the property. Also, when he is brought in by the mortgagee, he is more secured being brought by the party with the upper hand, compared to when he is brought in by the mortgagor. Usually, the complexity arises at the termination of the mortgage by foreclosure.

Under the Common law, there were various positions as to the stance of the lessee. [19] First, it was argued that when the mortgagee asserts possessory right and claims absolute title by a foreclosure action, it amounts to a termination of the lease. This argument was supported by the position that if the lease was not terminated, the mortgagor may defeat, in its entirety, the security of the mortgagee by granting a long term lease for an inadequate consideration. Another foundation of this position was the view that the mortgagor could not make a lease giving a greater right than that which he had or which will interfere with the right of the mortgagee.

Another school of thought opined that the mortgagee could adopt and recognize the lease in the event of foreclosure. The mortgagee could do this by creating a new lease or by a simple acknowledgement of lessee of the mortgagee as his landlord. This acknowledgment creates 'a tenancy at will' but can be converted to a periodic tenancy by payment and acceptance of rent.

A third position under the common law was that if the mortgagee commences a foreclosure action, the leasehold will be terminated. The mortgagee need not join the lessee in the action to evict him because the lessee is not beneficially interested in the claim secured or the estate mortgaged. This position is backed up by the opinion that the mortgagee had from inception had the right to possession. Consequently, the lessee is at best considered as a tenant at sufferance to the mortgagee, and may be summarily evicted.

The Common law position has been modified in some foreign jurisdictions. In New York for instance, the mortgagee is given an option to either terminate or preserve the lease. When the mortgagee wants to terminate the lease, he makes the lessee a party to the foreclosure proceedings. But if he seeks to preserve the lease, the lessee is not joined and the rights and obligations of the lessee remains the same as they would be following an assignment of the reversion by the mortgagor. Under the New York rule, a foreclosure judgment against the mortgagor does not automatically amount to an eviction (nor a constructive eviction). According to King S.J. [1942], the lessee thus cannot rely on the foreclosure to deny the mortgagor of the rents accrued to him. In Pennsylvania, the courts went a step further to consider the position of the lessee should the property be sold. It is held that the purchaser becomes the landlord except he terminates the lease directly. If the purchaser sues the lessee for rent, it is taken as a constructive confirmation of the lease.

5. Protection of the Lessee

Given the controversial position the lessee finds himself,

there are certain factors the lessee can put in place to ensure his position is not uncertain in the mortgage transaction. These include:

Inclusion of the Mortgagee in the Lease Agreement: At the onset of the lease, the lessee can request that as part of the consideration of the lease, the mortgagee should covenant not to evict him in the event of a foreclosure. This can be by means of a subordination agreement. In most cases, the mortgagee will consent to this when the lease arrangement is advantageous.

An Action for Breach of Covenant of Quiet Enjoyment: In the event that the mortgagee evicts the lessee after the foreclosure becomes absolute, the lessee also has an option to institute an action against the mortgagor for this breach when the eviction occurs before the expiration of the term of the lease. By virtue of this, the lessee can claim damages. However, these damages will be measured by the value of the unexpired term less the rents reserved. The court held in *Gan v. Clark*³⁵ that, the lessee can also get reimbursement of advanced rent from the surplus money got from the sale of the mortgaged property.

It is important to note that if the lease agreement contains a clause limiting the covenant of quiet enjoyment (that is, subjecting the lease to the mortgage), this option will not be available to the lessee as such prevents any form of liability against the mortgagor if the lessee is evicted by reason of a foreclosure of the mortgage.

The lessee must bear in mind that a claim for damages is subtle, in that the mortgagor who was unable to pay back the principal sum may not be solvent enough to pay the damages claimed.

6. Conclusion

The realm of contract recognize just two parties by reason of privity. Usually, in a mortgage transaction, this would have been the mortgagor and the mortgagee. However, given the multitude of rights available to both parties, the lessee can be introduced into their arrangement.

This paper has given a detailed conceptualization of the creation of leases in the realm of Mortgages. It has also examined the extent of rights the Mortgagor, Mortgagee, and the Lessee enjoy during a Mortgage period. Notably, it is submitted that the control of the lessee at any point in time depends on the Mortgage contract and relatively, who is in possession during the subsistence of the lease. As examined above, the Lessee's rights and obligations are unambiguous during the pendency of the Mortgage, but complexities arise when the Mortgaged property is sold or foreclosed while the lease subsists.

It has been further posited in our discourse above that in such circumstance, the lease could be confirmed by the Mortgagee by a simple acknowledgement thereby creating a

35 252 NY 92, 169 NE 100 [1929]

tenancy at will, or by an action for rent against the lessee. On the other hand, the lease could be terminated by the Mortgagee. The stiff probabilities of this instance under the Common law were examined, as well as the liberal modifications in Foreign Jurisdictions like New York and Pennsylvania in the United States of America. Noteworthy, it would appear that the Nigerian Laws are silent on this complexity. In solving the above, this paper forthrightly captures protective mechanisms that can be explored by the lessee namely, the inclusion of the Mortgagee in the Lease agreement, and an action against the Mortgagor for breach of the Covenant of Quiet Enjoyment when he is evicted before the expiration of the lease.

It is also advisable that the Lessee's solicitor performs due diligence on a lessor's title to confirm the absence of a mortgage encumbrance. This is because the mortgagor's lessee is the least protected party when conflict arises. If the lease of such encumbered property is inevitable, the lease agreement must be diligently prepared to ensure that protective measures are put in place for the least favoured party (the Lessee in this case).

It is submitted in finality that, in situations as explored above, it is difficult to always have a win-win situation for all three parties, but the rights of each party can be sufficiently protected to ameliorate or cushion total loss.

Conflicts of Interest

The authors declare no conflict of interest.

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