[HIGH COURT OF AUSTRALIA.]

SOUTHWELL . . . . . APPELLANT;
DEFENDANT,

AND

ROBERTS AND ANOTHER . . . . RESPONDENTS.
PLAINTIFF AND DEFENDANT,

ON APPEAL FROM THE SUPREME COURT OF NEW SOUTH WALES.

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SYDNEY, *Aug.* 7, 8; *Sept.* 10.

Starke, Dixon and McTiernan JJ.

Mortgage—Mortgagee in possession—Permanent improvements—Suit for redemption—Allowance of cost of improvements.

A mortgagee by memorandum of mortgage under the *Real Property Act* 1900 (N.S.W.) of property consisting partly of vacant land and partly of land whereon were erected two old and dilapidated semi-detached houses went into possession of the mortgaged property. While in possession he demolished the old houses and erected two new semi-detached cottages on the land whereon they had stood and a new cottage on the previously vacant land. The new buildings were suitable to the neighbourhood, and the work done considerably increased the capital and rental values of the mortgaged property; the cost of the demolition and the new buildings was greatly in excess of the amount secured by the mortgage.

Held, in a suit by the mortgagor for redemption, that, having regard to the disproportionate amount of the expenditure and the alteration which it produced in the nature of the mortgaged property, the mortgagee should not be allowed to add to the mortgage debt the cost of demolishing the old, and erecting the new, buildings.

Decision of the Supreme Court of New South Wales (*Nicholas* C.J. in Eq.); *Roberts* v. *Southwell*, (1940) 57 W.N. (N.S.W.) 33, affirmed.

APPEAL from the Supreme Court of New South Wales.

A suit by way of statement of claim was brought in the equitable jurisdiction of the Supreme Court of New South Wales by William Lester Roberts against Ruby Sarah Southwell and William Joseph

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Hanly for the redemption of a mortgage of a parcel of land situate at Lucy Street, Ashfield.

The mortgage was given to the defendant Southwell on 10th August 1928 to secure the repayment of a sum of £850 with interest thereon, and contained the covenants usual in a memorandum of mortgage under the *Real Property Act* 1900 (N.S.W.).

About June 1931 the defendant Southwell, as mortgagee, went into possession of the land. At that time the land was subject to a second mortgage which had been given by the plaintiff to the defendant Hanly to secure repayment of the sum of £200 with interest thereon.

The land was divided into two parts, marked "A" and "B" on a plan approved by the municipal council and having frontages respectively of fifty-four feet eleven inches and thirty-three feet to Lucy Street, Ashfield. On portion "A" were two semi-detached brick houses. Portion "B" was vacant land. In 1928 the two houses were kalsomined, the woodwork was painted and the paths repaired, but in 1932 and in 1936 neither of the houses was in good repair. They were old buildings, the timber was infested with white ants and borers, most of the timber being pine, and in the opinion of the municipal council's health inspector the most prudent course economically for an owner to take either then or shortly afterwards would have been to demolish and rebuild the houses. The mortgagee caused the houses to be repaired in 1933. In 1936 her representative estimated that it would cost about £200 to put the houses in repair and decided to have them demolished and to erect other buildings on the whole of the land. In pursuance of this decision the old houses were demolished at a cost of £60 and a double-fronted brick cottage, containing four rooms, cooking recess and offices, with a tile roof, was erected partly on portion "B" and partly on portion "A," and on the balance of portion "A" were erected two brick bungalow flats—in the statement of claim referred to as two semi-detached brick cottages—each containing four rooms, cooking recess and offices, with tile roof and two garages. The expenditure on the new buildings was £1,640. It represented the cost of labour and materials, but use was also made of materials from the old buildings. The new buildings were suitable to the

neighbourhood and, as compared with the old buildings, would command increased rentals.

It was not shown that the consent of the mortgagor was obtained before these buildings were erected or that he had had notice of the proposal and had acquiesced therein.

A valuation made by the Valuer-General on 13th July 1934 showed that the unimproved value of the land was then £440; the improved value, £650; and the assessed annual value, £70. The land was again valued by the Valuer-General on 19th August 1937, after the old buildings had been demolished and the new buildings erected. The unimproved value of that part of the land upon which the double-fronted brick cottage had been erected was shown as £203; the improved value as £950; and the assessed annual value as £76. The unimproved value of the balance of the land, being that part upon which the two brick bungalow flats had been erected, was shown as £280; the improved value as £1,600; and the assessed annual income as £152.

It appeared from the correspondence between the solicitors for the parties that the mortgagor in order to redeem proposed to tender a sum of approximately £1,166, being the amount owing under the mortgage in respect of principal, interest and other minor charges, less rents received, and that if the mortgagee were entitled to debit him with the cost of the demolition of the old buildings and the erection of the new buildings, or with the amount by which the value of the mortgaged property had been increased by the erection of these buildings, he must pay an additional sum of £1,700.

The trial judge held that, although the value of the subject property had been increased by her action, the mortgagee was not entitled to add to the mortgage debt the costs or expenses incurred by her in demolishing the old buildings or any costs or expenses incurred by her in erecting the new buildings. The matter was referred to the Master in Equity to take an account (*a*) of principal, interest and costs due by the plaintiff to the defendant under the mortgage, (*b*) of the rents and profits of the premises originally erected on the land which were received, or which without her wilful default might have been received, by the defendant up to the date of demolition, and of the rents and profits which in the opinion of the Master in

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Equity would have been received by her thereafter up to the date of the decree if the premises had not been demolished, and (*c*) of the amount which in his opinion would have been received by the defendant between the date of the decree and the date fixed for the payment of the mortgage debt in respect of the rents and profits of the said premises had they not been demolished. The amount found to be due under *b* was ordered to be deducted from the amount found to be due under *a*, and from the balance so found was to be deducted the amount found under *c*: *Roberts* v. *Southwell* (1).

From this decision the mortgagee appealed to the High Court.

The defendant Hanly did not enter an appearance, nor did he appear, by himself or by counsel, either at the trial of the suit or upon the hearing of the appeal.

Barwick (with him *Kenny*), for the appellant. A mortgagee is entitled to be allowed in account in redemption the cost or value, whichever is the lesser, of such lasting improvements as did in fact increase the value of the mortgaged property (*Henderson* v. *Astwood* (2)), provided (*a*) that such improvements did not change the nature of the property, or the purposes to which it was put, and (*b*) that the amount of the cost or value so allowed is not so incommensurate in the circumstances as to be an effective bar to the redemption of the property by the mortgagor (*Sandon* v. *Hooper* (3)). A mortgagee is entitled to reasonable expenditure on lasting improvements (*Shepard* v. *Jones* (4); *Tipton Green Colliery Co.* v. *Tipton Moat Colliery Co.* (5); *Coote* on *Mortgages*, 9th ed. (1927), vol. 2, pp. 1229, 1230; *Fisher and Lightwood's Law of Mortgage*, 7th ed. (1931), p. 728), including improved new buildings erected in substitution for old defective buildings (*Marshall* v. *Cave* (6); *Powell* v. *Trotter* (7)). The function of the court does not rest so much upon principle as upon the requirement to do what is just and equitable between the two parties (*Quarrell* v. *Beckford* (8)). The absence of consent or knowledge on the part of the mortgagor is not a reason

(1) (1940) 57 W.N. (N.S.W.) 33.
(2) (1894) A.C. 150, at p. 163.
(3) (1843) 12 L.J. Eq. 309, at p. 310; (1844) 14 L.J. Eq. 120.
(4) (1882) 21 Ch. D. 469, at p. 476.
(5) (1877) 7 Ch. D. 192.
(6) (1824) 3 L.J. (O.S.) Ch. 57.
(7) (1861) 1 Dr. & Sm. 388 [62 E.R. 428].
(8) (1816) 1 Madd. 269, at p. 281 [56 E.R. 100, at p. 104].

why expenditure by a mortgagee on permanent improvements should not be allowed (*Powell* v. *Trotter* (1)). Notice to the mortgagor is not necessary if the improvement is a reasonable one and produces a benefit (*Shepard* v. *Jones* (2)). The appellant is only chargeable with net rent. The cost of keeping the old buildings in tenantable repair should be allowed.

Myers, for the respondent. The test of reasonableness is : What is reasonable as regards the mortgagor ? A mortgagee is not entitled to change the character or nature of the mortgaged property (*Shepard* v. *Jones* (3) ; *Moore* v. *Painter* (4) ; *Woods* v. *Robertson* (5)), or to make it impossible or difficult for the mortgagor to redeem the property. It is never reasonable in any circumstances for a mortgagee to cause a building to be erected on mortgaged vacant land and thus to alter the character of the mortgaged property. The court disallows lasting improvements even though they are not grossly disproportionate (*Bright* v. *Campbell* (6)). In any event a mortgagee cannot get more than the increase in value or the amount expended by him, whichever is the lesser. The matter to be considered is the character of the property before as compared with after the expenditure was made ; the amount expended and the relation of that amount to the nature and value of the property. For this purpose increase in value has nothing to do with reasonableness. In *Marshall* v. *Cave* (7) only a very dilapidated kitchen, pantry, &c.—not a complete house—were demolished and rebuilt. The propriety of the improvements was not disputed by the mortgagor in *Henderson* v. *Astwood* (8). What a mortgagee is entitled and not entitled to do is shown in *Sandon* v. *Hooper* (9). The appellant is not entitled to a decree giving her the benefit of amounts which she would have expended in maintaining the property in a proper state of repair because the amount of such expenditure cannot be assessed. The decree should either remain in its present form or it should be the ordinary decree with a direction similar to

(1) (1861) 1 Dr. & Sm., at p. 390 [62 E.R., at p. 428].
(2) (1882) 21 Ch. D., at p. 479.
(3) (1882) 21 Ch. D., at p. 482.
(4) (1842) 6 Jur. 903.
(5) (1901) 21 N.Z.L.R. 137.
(6) (1885) 54 L.J. Ch. 1077.
(7) (1824) 3 L.J. (O.S.) Ch. 57.
(8) (1894) A.C. 150.
(9) (1843) 6 Beav. 246, at p. 248 [49 E.R. 820, at p. 821].

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the direction given in *Bright* v. *Campbell* (1). "Net" rent is not objected to.

Barwick, in reply. *Moore* v. *Painter* (2); *Bright* v. *Campbell* (3), and *Woods* v. *Robertson* (4) are cases of changing the nature of the property. In the circumstances the action taken and the amount expended were reasonable. The improvements effected come within the decision in *Shepard* v. *Jones* (5).

Cur. adv. vult.

Sept. 10.

The following written judgments were delivered:—

STARKE J. This was a redemption suit brought in the Supreme Court of New South Wales by a mortgagor against a mortgagee in possession of the mortgaged property. The mortgagor—the respondent here—claimed that the mortgagee—the appellant here—was not entitled to add to the amount due and owing to her under and by virtue of the mortgage of certain land any costs and expenses incurred by her in demolishing houses erected on the land comprised in the mortgage or any costs and expenses incurred by her in making certain permanent and lasting improvements on the land. A declaration was made accordingly: hence this appeal.

A mortgagee in possession must act as a provident owner. He has no right to improve the mortgagor out of his property (*Sandon* v. *Hooper* (6); *Shepard* v. *Jones* (7)). There is nothing, as Lord *Langdale* said in *Moore* v. *Painter* (8), "more necessary for this court to do than to take care that a mortgagee in possession shall so deal with the mortgaged property as to be able to restore it to the mortgagor in the same nature as he receives it." He may be allowed proper and necessary repairs to the estate. He has been allowed to complete buildings which were uncompleted and to pull down buildings that have become ruinous and unfit for use, and even to substitute new buildings for those which were too ruinous to be any longer useful (*Marshall* v. *Cave* (9)). And he may be allowed permanent and lasting improvements which produce a benefit to

(1) (1885) 54 L.J. Ch., at p. 1078.
(2) (1842) 6 Jur. 903.
(3) (1885) 54 L.J. Ch. 1077.
(4) (1901) 21 N.Z.L.R. 137.
(5) (1882) 21 Ch. D. 469.
(6) (1843) 12 L.J. Eq. 309; 14 L.J. Eq. 120.
(7) (1882) 21 Ch. D. 469.
(8) (1842) 6 Jur., at p. 905.
(9) (1824) 3 L.J. (O.S.) Ch. 57.

the property and are reasonable in amount and reasonable having regard to the nature of the property (*Shepard* v. *Jones* (1); *Woods* v. *Robertson* (2)). Otherwise the mortgagee should protect himself by obtaining the consent or acquiescence of the mortgagor (*Shepard* v. *Jones* (1)).

Shortly the facts of the case are :—1. The mortgage was given in 1928 to secure the sum of £850 and interest thereon. 2. On portion of the mortgaged land two semi-detached houses were erected : the other portion was vacant. The buildings were of an old-fashioned type. At the time of the mortgage they had been put in fair repair and could command tenants who could only afford to pay inconsiderable rentals. 3. The mortgagee went into possession in 1931. At that time the amount owing to him under the mortgage was £995 and the mortgagor had not met rates and other outgoings. 4. In 1934 a valuation of the Valuer-General stated the improved capital value of the land to be £650 and the annual value £70. 5. The mortgagee effected some repairs between 1932 and 1936, but in 1936 it was estimated that it would cost a sum of about £200 to put the premises in repair. 6. The buildings at that time were dilapidated and the timber infested with white ants and borer and the most prudent course economically would have been to pull them down and rebuild. 7. About 1936, the mortgagee did demolish the buildings at a cost of £60 and erected a pair of semi-detached brick cottages on one portion of the land and a three-quarter front detached brick bungalow on the other. The expenditure on the new buildings, excluding the cost of demolition, was £1,640. It represented the cost of labour and materials, but use was also made of materials from the old buildings. 8. The new buildings were suitable to the neighbourhood and would command tenants at increased rental. 9. In 1937, a valuation of the Valuer-General stated the improved capital value of the land to be £2,550 and the annual value £228.

The learned trial judge concluded on these facts that the expenditure of the mortgagee in rebuilding, though it had increased the value of the land, was not an expenditure with which the mortgagor should be charged.

(1) (1882) 21 Ch. D. 469.

(2) (1901) 21 N.Z.L.R. 137.

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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 possibly by foreclosing.

The decree also directs an account of rents and profits based upon *Bright* v. *Campbell* (1), but the parties agreed that the account should be of net profits. The variation is, I think, unnecessary, but as the parties have agreed the decree may be varied accordingly.

Subject to this variation this appeal should be dismissed.

DIXON J. This appeal is concerned with the allowance to a mortgagee in possession of the cost of effecting permanent improvements to the mortgaged property without the consent or acquiescence of the mortgagor. The facts, which have already been fully stated in the judgment of *Starke* J., show that old and undesirable buildings have been demolished and that houses have been erected at great cost, giving the mortgaged land a value perhaps three or four times that which it possessed before, but involving a considerable alteration in the particular character of the premises. The question whether an expenditure of this nature should be allowed to the mortgagee and added to the mortgage debt requires a choice between two courses, neither of which can be regarded as altogether satisfactory. For, on the one hand, to disallow the expenditure means that the mortgagor obtains at the expense of the mortgagee and without any merit on his part a very large increase in the value of the property he redeems; while, on the other hand, to allow it is to sanction a dealing by the mortgagee with the mortgaged premises never contemplated by the security, one which might be quite

(1) (1885) 54 L.J. Ch. 1077.

opposed to the mortgagor's desires and, perhaps, inconsistent with his plans and even with his business necessities, and one imposing upon him an obligation to find a very much larger sum than he borrowed before he can redeem his property.

The choice between these courses is made no less unsatisfactory and difficult by the very vague and indefinite standard provided by the case law for determining when expenditure upon substantial and permanent alterations or " lasting improvements " may not be allowed in the accounts of a mortgagee in possession and when it is allowable.

We are not of course concerned with the cost of maintenance or ordinary repairs of a recurrent character. The question relates to substantial or structural changes of a lasting description. The authorities dealing with such a question are not numerous and it appears desirable to set out the effect of the chief decisions in order.

1. It appears that, at the close of the eighteenth century, in a decree of redemption where the mortgagee was in possession it was not unusual to include an account of repairs and lasting improvements and interest on such improvements after the rate the mortgage carried, the amount to be added to the mortgage debt. But such a provision does not seem to have been part of the common decree for redemption: it was a special direction: See the decree in *Spurgeon* v. *Collier* (1) and in *Stephenson* v. *Green* (2); *Gubbins* v. *Creed* (3).

2. In *Hardy* v. *Reeves* (4), Lord *Alvanley* remarked that he had no difficulty in saying that the mortgagee of a copyhold may take down ruinous houses and may build much better houses. But he added that the lord had a right to say that the tenant should not let the houses fall, and might seise if he did. And this shows that the nature of copyhold tenure entered into Lord *Alvanley's* reason for the observation.

3. In *Marshall* v. *Cave* (5) a case arose before Sir *John Leach* V.C. of a mortgagee in possession who had rebuilt a " kitchen, pantry,

(1) (1758) 1 Eden 55, at p. 63 [28 E.R. 605, at p. 607].
(2) (1801) *Seton* on *Decrees*, 3rd ed. (1862), vol. 1, p. 474.
(3) (1804) 2 Sch. & Lef. 214, at p. 224 [9 R.R. 71, at p. 76].
(4) (1799) 4 Ves. 466, at p. 480 [31 E.R. 239, at p. 246].
(5) (1824) 3 L.J. (O.S.) Ch. 57.

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&c." and had had a house double-roofed instead of being, as it was before, only single-roofed. The report says no more about the nature of the premises than that it was a mortgage of a house and appurtenances; the amount of the mortgagee's expenditure on the alterations is not given. The Vice-Chancellor overruled an exception to the Master's report, allowed the cost of the improvement in the accounts of the mortgagee, and said:—"This mortgagee has not made new buildings for new purposes; he has only directed new buildings on the site of the old, and for the same purposes as were served by them. The new buildings are mere substitutions for those which were too ruinous to be any longer useful" (1).

4. In *Moore* v. *Painter* (2) certain messuages malt-houses and premises in Birmingham had been mortgaged to secure £700. The mortgagee entered into possession and retained possession for some twenty years, when a suit for redemption was brought. A decree was made which included a direction to take an account of all sums of money paid, laid out and expended by the mortgagee on repairs and lasting improvements on the estate and premises comprised in the mortgage security. The Master's report showed that the mortgaged premises had consisted of two houses fronting a street, a small house on the east side, a slaughter-house, a stable and other premises and two malt-houses. At the time the mortgagee took possession one of the front houses was let as a butcher's shop and the other shop and the malt-houses were let to various tenants. After a time the butcher's shop and slaughter-house and other parts of the premises became untenanted and their condition was considered dangerous. They were demolished, and some time afterwards the remainder of the premises was taken down and an iron warehouse built on the site. The two malt-houses were converted into one warehouse. The mortgagees claimed an allowance of sums amounting to somewhat more than £1,000 for those improvements, but the Master disallowed them, "being of opinion that the defendants were not authorized to convert the said dwelling-houses into an iron warehouse" (3). Exceptions to the report were made, and they came before Lord *Langdale* M.R. His Lordship said:—"It is immaterial

(1) (1824) 3 L.J. (O.S.) Ch. 57. (2) (1842) 6 Jur. 903.
(3) (1842) 6 Jur., at p. 904.

whether the shops were or were not in a ruinous condition. He made great alteration in the nature of the property, and though he might by so doing make the property more valuable, yet did he as mortgagee stand in such a position with reference to the mortgagor, that, having a right to make repairs, which the court would allow, he had a right to convert the property to a purpose entirely different? There is nothing more necessary for this court to do than to take care that a mortgagee in possession shall so deal with the mortgaged property as to be able to restore it to the mortgagor in the same nature as he receives it. Here there was a conversion of shops open to the street into an iron warehouse. In 1835, that which was an improved malt-house was converted into an iron warehouse. The mortgagee did not pull it down, but he connected the two buildings, and converted that property which formerly consisted of shops and two malt-houses into one entire warehouse. It might be a great improvement of the property, but it was not one in my opinion which the mortgagee was entitled to make, and in this I concur with the Master. It may be a case of great hardship, but my opinion proceeds on the relation between mortgagor and mortgagee" (1).

5. In *Sandon* v. *Hooper* (2) Lord *Langdale* M.R. and on appeal Lord *Lyndhurst* L.C. disallowed the costs of removing some dilapidated cottages and erecting some other structure on the site. The mortgaged property consisted of two cottages with half an acre of pasture land adjoining and another cottage, licensed as a public house, on a site of four and a half perches with pasture adjoining. The mortgagee entered into possession and pulled down the two cottages which, it is said, appeared by the evidence not to be in such a state of dilapidation that they required pulling down. The mortgagee claimed that he had effected lasting improvements on the mortgagor's property, but, according to one report, he is said to have built a hovel instead. According to another, he is said to have built a stable attached to the public house and, in the argument of the mortgagor's counsel, to have rebuilt the cottages but unnecessarily. Lord *Langdale* M.R. said:—"The cases in the books very

(1) (1842) 6 Jur., at p. 905.
(2) (1843) 6 Beav. 246 [49 E.R. 820]; 12 L.J. Ch. 309; 14 L.J. Ch. 120.

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clearly point out what a mortgagee in possession ought to do with reference to repairs, and what he ought not to do; the expenses incidental to necessary repairs a mortgagee will always be allowed in account, as also any costs incurred by him in preserving the estate, and in protecting the title of the mortgagor; and if in the course of his expenditure he has done only what is fit and proper to be done, and he has the consent thereto of the mortgagor, or the mortgagor acquiesces in what the mortgagee does, the latter will be allowed sums laid out in substantially improving and increasing the value of the estate; but the mortgagee has no right to increase the value of the estate to such extent as to improve the mortgagor out of the same, as is the common expression, or, in other words, to place it out of the power of the mortgagor to redeem the property. In short, the expenses incurred by a mortgagee ought to be such only as will preserve the property, and protect the title of the mortgagor thereto; and in bills filed to redeem, it is not a matter of course to direct an inquiry, whether any sums have been laid out by the mortgagee in substantial repairs and lasting improvements; but, if the fact be, that sums have been expended by the mortgagee on the property (and it is not requisite to prove detailed items of outlay), then it is proper that such an inquiry should be granted; but in the case before me there is a total absence of evidence on the part of the defendant, in support of his allegation of the expenditure of any sums in substantial repairs or lasting improvements" (1). In affirming this judgment Lord *Lyndhurst* L.C. said:—"The mortgagee enters and makes improvements and repairs; but, at the same time, pulls down part, and puts something else in lieu of it. The whole of this must be taken together, and the question is, what is the result? The result, taking the whole, is that the premises have been injured. I cannot, therefore, take the repairs and lasting improvements, and refer it to the Master to inquire how much the mortgagee is entitled to for them. I must take the case together, and if the value of the property is not increased, there can be no ground for such a reference to the Master" (2).

6. In *Shepard* v. *Jones* (3) a comparatively small expenditure was in question. The principal sum secured by the mortgage was £4,000, and the mortgaged property was a brewery. The mortgagee in possession spent £83 in deepening a well in order to obtain a better

(1) (1843) 12 L.J. Ch., at pp. 310, 311. (2) (1844) 14 L.J. Ch., at pp. 120, 121.
(3) (1882) 21 Ch. D. 469.

supply of water. He afterwards sold the premises in the exercise of his power of sale. The mortgagor's action was consequently for an account and the surplus purchase money, not for redemption. The Court of Appeal directed an inquiry whether any and what sum ought to be allowed in taking the accounts of the mortgagee by reason of lasting improvements. Sir *George Jessel* M.R. distinguished between the amount of proof in a redemption suit entitling a mortgagee to an inquiry as to lasting improvements and that entitling him to an account of the expenditure. If the mortgagee, having pleaded that he has laid out money in lasting improvements, gives general evidence, he may obtain an inquiry. If he goes on to prove that the property has been improved to an amount equal to or greater than the expenditure he may then obtain an account. He considered that a foundation for an inquiry had been laid in respect of the well. But he went on to make a further distinction. He distinguished between a redemption suit and a suit for the surplus proceeds of a sale of the mortgaged property. "If it should turn out that the mortgagee has done something to the property at his own expense which increased its saleable value, I think it is plain on ordinary principles of justice, that that increase should not go into the pocket of the mortgagor without his paying the sum of money which caused the increase" (1).

Cotton L.J. (2) decided that the expenditure should be allowed on the ground that it was reasonably done for the purpose of improving the actual state of the property, not an alteration but improving it for the purpose of carrying out the object of the mortgagee, namely, to realize it by sale. At the same time the Lord Justice stated that a mortgagee may not lay out a very large sum when in possession and throw a great burden on the mortgagor and may not alter the nature of the property. He regarded the expenditure as reasonable in amount and reasonable with reference to the existing purposes of the property and as prima facie increasing the value for the purpose of sale.

An explanation was given of the observation of Lord *Langdale* in *Sandon* v. *Hooper* (3) to the effect that if the mortgagee has got the

(1) (1882) 21 Ch. D., at pp. 477, 478. (2) (1882) 21 Ch. D., at p. 483.
(3) (1843) 12 L.J. Ch., at pp. 310, 311.

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consent of the mortgagor or has given him notice in which he acquiesces, then he may be allowed sums of money laid out in increasing the value of the mortgaged property. The necessity of the consent or acquiescence of the mortgagor is limited to cases where the expenditure is upon substantial works, buildings, or alterations which are unreasonable or produce no benefit. Reasonable improvements productive of actual benefit may be allowed independently of the mortgagor's consent or acquiescence. But the mortgagee cannot burden the mortgagor with unreasonable expenditure simply by notifying him.

7. In *Henderson* v. *Astwood* (1) the Privy Council directed an inquiry whether to a mortgagee of a wharf who had validly exercised his power of sale any and what sum ought to be allowed in respect of lasting improvements. The purchaser was named Henderson and the mortgagee Davies. Lord *Macnaghten* said :—" That Davies did make lasting improvements was admitted. It was not disputed that those improvements were necessary and proper, and that they added to the value of the premises. It would be contrary to common justice to deprive Davies of the benefit of the money laid out by him on those improvements, so far as they enhanced the value of the premises. Following the decision of Sir *George Jessel* M.R., in the case of *Shepard* v. *Jones* (2), their Lordships think that an inquiry should be directed in general terms to ascertain what sum ought to be allowed in respect of lasting improvements. It was said that the improvements which Davies made could not have added to the value of the property from Henderson's point of view, having regard to the purpose for which he wanted it. That may be very true, but still Henderson may have had to pay a larger price for the premises because they were fitted with modern improvements, and suited to the ordinary requirements of the trade of the port " (3).

8. In *Bright* v. *Campbell* (4) a suit for redemption was brought by the second mortgagees of a freehold dwelling-house, factory and premises. The first mortgagee had gone into possession. One Betts had been in occupation of the property as tenant of the mortgagor

(1) (1894) A.C. 150.
(2) (1882) 21 Ch. D. 469.
(3) (1894) A.C., at p. 163.
(4) (1885) 53 L.T. 428 ; 54 L.J. Ch. 1077.

and the first mortgagee purported to sell the property to him. Notwithstanding the purported sale a decree for redemption was made. After the decree Betts remained in possession and expended £5,200 in erecting additional buildings on part of the mortgaged property for the purpose of developing the factory business which he there carried on. A great increase resulted in the value of the property. Betts was treated as occupying under the first mortgagee and as standing in his position. It was claimed that the increase in value or the expenditure should be allowed in the taking of accounts. *Cotton* L.J. said :—" The property has no doubt increased in value owing to the expenditure of Betts, but, in my opinion (although we do not decide that point now), he cannot successfully contend that this expenditure, which has entirely altered the character of the property, ought, in taking the account, to be allowed him as against the second mortgagee. But then Betts says that, if this expenditure is not to be allowed to him, at all events an increased rental ought not to be put upon the property when the increase in its value is attributable to the expenditure which he has himself made ; and, in my opinion, he is right there. The second mortgagee cannot be allowed to make that expenditure a reason for throwing a greater burden on the first mortgagee by increasing the sum with which the first mortgagee is to be charged as an occupation rent. In my opinion, it would be contrary to all principles of equity to allow that. I think that the appellant is right on this point, and that there should be a direction that, in fixing the amount of rent in respect of the mortgaged property, no addition is to be made by reason of any increase in value attributable to any additional buildings or erections or alterations of, or lasting improvements to the existing buildings made therein by the first mortgagee since the date of the decree, the expenditure for which is not, however, to be allowed to him " (1).

9. In *Woods* v. *Robertson* (2) a vacant piece of land was equitably mortgaged to secure a small loan. The mortgagor disappeared and after some time the mortgagee erected buildings on the land costing £200 and went into occupation of the premises. The mortgagor

(1) (1885) 53 L.T., at p. 430.

(2) (1901) 21 N.Z.L.R. 137.

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died and his legal personal representative brought a suit for redemption. *Williams* J. held that the mortgagee was not entitled to add to the security the cost of the improvements. Referring to *Shepard* v. *Jones* (1), he said :—" In that case, however, it was held that in order to justify such an inquiry the mortgagee must show some prima-facie evidence—first, that he had incurred an expenditure; secondly, that it was incurred in a matter which, prima facie, might be an improvement of the property; thirdly, that such improvement would be a lasting improvement; and, fourthly, that such expenditure was a reasonable expenditure. In the present case we have evidence on the first three points, but the evidence as to the fourth point, I think, shows that the expenditure was unreasonable. The test of reasonableness is given by *Cotton* L.J., in the above case (1). The expenditure must be reasonable in amount and reasonable with reference to the existing purposes of the property. The same learned judge also says :—' A mortgagee has no right as against a mortgagor to improve the mortgagor out of his property, and if he lays out a very large sum, that is in itself a thing which he has no right to do. A mortgagor must not be prevented from redeeming by the mortgagee when in possession throwing a great burden on him.' These principles have been always recognized " (2).

10. In *Lamacraft* v. *Smith* (3) *Neville* J. allowed an improvement by a mortgagee in possession of leasehold premises and directed that the increased annual value of the premises should be capitalized at ten per cent per annum as from the time of the increase to the termination of the lease. The mortgaged property included a dwelling house occupied by a tenant who refused to renew his tenancy unless the mortgagee would build a workshop at the back of the house to enable him to carry on his business of a tobacco-pipe manufacturer. The mortgagee did so at a cost of £272 and thereby secured an addition of £10 to the rent. The loan secured originally was £350.

11. In *Manitoba Lumber Co. Ltd.* v. *Emmerson* (4) a mortgagee of a timber mill entered into possession as mortgagee, but under an

(1) (1882) 21 Ch. D. 469.
(2) (1901) 21 N.Z.L.R., at pp. 140, 141.
(3) (1916) 140 L.T. Jo. 501.
(4) (1912) 5 D.L.R. 337.

arrangement by which the mortgagor was to be credited with $200 a month for the use of the mill. The mill was then pulled down by the mortgagee or with his sanction and another built at an expenditure of $106,000. In the Supreme Court of British Columbia, *Gregory* J. considered that the mortgagee never intended the mortgagor to redeem and deliberately set to work to improve the mortgagor out of his property and make it impossible to redeem. Under all heads, the indebtedness secured by the mortgage finally amounted to $51,000. *Gregory* J. (1) said that the statement of *Cotton* L.J. in *Shepard* v. *Jones* (2) was peculiarly applicable, viz., that a mortgagee had no right to lay out a very large sum and prevent a mortgagee from redeeming by throwing a great burden upon him; but he included in his decree an account of the moneys expended by the defendant in necessary or reasonable repairs.

12. There are a few other examples of the invocation of the principle in the dominions, but they are less in point: See, for example, *Waterloo Manufacturing Co.* v. *Holland* (3); *Smyth* v. *Dalgety & Co.* (4); *Donovan* v. *Hanna* (5).

The foregoing account of the decided cases appears to show that courts of equity refrained from formulating any precise test for determining what description of improvements might be made by a mortgagee in possession at the charge of the mortgagor. The decisions do no more than establish what are the considerations that must be taken into account and leave to be judged on the facts of the particular case the question whether having regard to those considerations the expenditure was fair, reasonable and proper.

The matters upon which this determination is to be made may be stated thus:—

The first consideration is the amount of the mortgage debt and the proportion which the expenditure bears to it. A mortgagee is a creditor who enjoys rights in the mortgaged premises only for the purpose of securing repayment. He ought not to be allowed under colour of protecting and effectuating his security to burden the property with a debt out of all relation to the principal sum borrowed or the mortgage moneys owing at the time.

(1) (1912) 5 D.L.R., at p. 346.
(2) (1882) 21 Ch. D. 469.
(3) (1917) 36 D.L.R. 216.
(4) (1892) 13 L.R. (N.S.W.) Eq. 20.
(5) (1926) N.Z.L.R. 883.

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Closely related to this consideration is the effect produced upon the mortgagor's ability to redeem. The mortgagee ought not to be allowed against the mortgagor expenditure so disproportionate to the mortgage moneys and so out of keeping with the value of the security and of the equity of redemption that the mortgagor may be hampered in redeeming the property.

Then the character of the mortgaged premises must be considered. Changes are not to be made in buildings or otherwise which radically alter the nature or useful purpose of the property. However much the value is increased, the mortgagor is entitled, on redemption, to have restored to him the substance of the thing he has mortgaged.

A further consideration is the permanence of the improvement. A mortgagee cannot charge expenditure on things, other than maintenance and repairs, which do not or may not outlast his own possession or enure for the actual benefit of the mortgagor and those claiming under him. Then the effect of the expenditure upon the value of the property is important. The mortgagee in possession cannot load the security with expenditure which is not represented in the enhanced value which it has given the premises.

These, however, are matters not in themselves affording decisive tests but providing the considerations upon which the reasonableness of the conduct of the mortgagee in effecting the improvements is to be judged. His own position is, of course, not to be left out of account. But he is to be considered, not as a potential owner, but as a creditor looking to a security as a means of repayment.

Upon the facts in the present case there can, I think, be only one conclusion when these matters are regarded. The disproportionate amount of the expenditure and the alteration in the nature of the premises produced by demolishing the old buildings and erecting new semi-detached cottages on the vacant portion of the land and a single cottage on the site of the former building combine to make it impossible to allow the mortgagee to add the cost to the mortgage moneys.

It is no doubt very unfortunate for the mortgagee, and at the same time there can be almost as little doubt that the result to the mortgagor is a windfall. But the loss to the mortgagee arises altogether from her ignoring the mortgagor's position and proceeding

to build upon the tacit assumption that she was an absolute owner and not simply a mortgagee in possession of a security for a debt.

The decree, at all events with the insertion of the word "net" before "rents and profits" in the direction for the account of what revenue the mortgagee ought to have derived from the property, accords with *Bright* v. *Campbell* (1) and *Donovan* v. *Hanna* (2).

In my opinion the appeal should be dismissed with costs.

McTiernan J. The mortgage in this case was made by a memorandum of mortgage which was registered under the provisions of the *Real Property Act* 1900. Upon registration of the memorandum the land comprised in it became, by virtue of sec. 41 of the Act, liable as security in the manner and subject to the conditions set forth in the instrument or declared by the Act to be implied in instruments of a like nature. The first inquiry, then, is whether there is any such express or implied condition charging the mortgaged land with the moneys which the mortgagee expended in demolishing the old semi-detached houses and in building the new dwellings on the land. The repairs which the mortgagor was bound by his covenant to perform were described in the memorandum as necessary repairs; and it was an express condition that, if he failed to perform this covenant, any moneys which the mortgagee expended in doing repairs necessary to keep buildings in tenantable condition should be charged on the land. The works of demolition and building which the mortgagee did were not repairs of this character. In mortgagee's accounts a sharp distinction is made between moneys expended on necessary repairs and expenditure on permanent and lasting improvements (*Tipton Green Colliery Co.* v. *Tipton Moat Colliery Co.* (3); *Houghton* v. *Sevenoaks Estate Co.* (4)). The work done by the present mortgagee belongs to the latter category. As to the Act itself, a condition charging the cost of this work on the land cannot be implied from its provisions. The mortgagee, therefore, has no contractual right to be allowed any part of this expenditure.

The next inquiry is whether the expenditure should be allowed on equitable grounds. "A court of equity considers itself competent

(1) (1885) 54 L.J. Ch. 1077.
(2) (1926) N.Z.L.R. 883.
(3) (1877) 7 Ch. D. 192.
(4) (1884) 33 W.R. 341.

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in this relation between mortgagor and mortgagee to go beyond the contract—to consider what is just and equitable between parties, standing in that relation " (*Quarrel* v. *Beckford* (1)). In redemption proceedings relief is sought on equitable considerations and the court may consider it just and equitable to impose upon a mortgagor as the price of the redemption of the security the obligation of paying a sum of money exceeding his contractual liability. In going outside the contract the court exercises its power " to put its own price upon its own interference as a matter of equitable consideration in favour of any suitor " (*Cummins* v. *Fletcher* (2)). Hence equity allowed in the accounts of a mortgagee in possession moneys expended on permanent or lasting or substantial repairs if it was just and equitable to do so. In *Marshall* v. *Cave* (3) a mortgagee, who had taken possession, was allowed the expense of buildings substituted for decayed old buildings, even though the new buildings were on an improved scale. The new buildings were erected " on the site of the old and for the same purposes as were served by them." It appears from the exception taken to the Master's report in that case (3) that the improvements were made without the sanction of the mortgagor. The reported cases, which are remarkably few, contain considerations upon which the court of equity acted in allowing or refusing to allow the cost of permanent or lasting improvements. These cases have been reviewed by my brother *Dixon* and it is unnecessary to set out again the tests applied in them. But, as the dominant consideration is what is just and equitable between mortgagor and mortgagee, these tests may not solve every case. In the present case the mortgagee without the mortgagor's sanction or acquiescence demolished the two semi-detached houses on the mortgaged land, erected in their place a new house, and on the vacant land, part of the security, adjoining the old houses built two new semi-detached houses, expending on all this work a sum vastly exceeding the amount of the mortgage debt. The work done brought about a permanent change in the nature of the security. The expenditure might, as the mortgagee endeavoured to show, have been provident because of the nature of the locality. Expenditure which is provident if made by an absolute owner might be

(1) (1816) 1 Madd., at p. 281 [56 E.R., at p. 104].

(2) (1880) 14 Ch. D. 699, at p. 708.

(3) (1824) 3 L.J. (O.S.) Ch. 57.

rash if incurred by a mortgagee in possession. The expenditure enhanced the value of the mortgaged property. But it would not, in my opinion, be equitable to allow the mortgagee the benefit of it in her accounts, because the right to do the work cannot be reconciled with the mortgagor's equity to redeem the property nor justified as necessary for the realization of the security.

In the case of a mortgage under the *Real Property Act* 1900, the question whether the cost of permanent improvements should be allowed in the accounts of a mortgagee may be affected by a number of provisions of the Act. Sec. 57 provides: "Any mortgage or encumbrance under this Act shall have effect as a security but shall not operate as a transfer of the land thereby charged." See also sec. 3, where "mortgage," "mortgagee" and "mortgagor" are defined, and sec. 41. The mortgagee exercised the power under the memorandum of mortgage to enter into possession of the property and to manage it in case the mortgagor made default. She did not take possession as the owner of the legal estate. The purpose of the power to enter and manage the mortgaged property is the realization of the security. In *Hooper* v. *Cooke* (1) the question arose as to the rights of the owner of a rent-charge who went into possession of the encumbered property to lay out money as a mortgagee in possession under a common-law mortgage and to alter the character of the property. Sir *John Romilly* M.R. said:—"The distinction between this case and a mortgagee in possession is this:—At law the mortgagee is absolute owner of the land, and has a right to deal with it as he thinks fit. The mortgagor comes to recover possession, notwithstanding his title at law is gone, but equity only gives relief on certain conditions, and will not give him possession, unless on the terms, not only of repaying all money due, but also all moneys which the mortgagee may properly have expended for the purpose of the sustaining and repairing the property. The owner of the rent-charge has no estate in the land, he has only a right of entry, and, by perception of the rents, to pay off the arrears; he is entitled to enforce payment of his rent-charge only in that peculiar way. On the other hand, the owner of the estate subject to the rent-charge is not bound to have resort to equity, but when

(1) (1855) 20 Beav. 639 [52 E.R. 750].

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the arrears have been paid, he can obtain possession without coming to a court of equity" (1). Sec. 58 (3) provides how the proceeds of the sale of the mortgaged property are to be applied when it is sold by the mortgagee in exercise of his power of sale. The section says: "The purchase money to arise from the sale of any such land, estate, or interest, shall be applied, first, in payment of the expenses occasioned by such sale; secondly, in payment of the moneys which may then be due or owing to the mortgagee or encumbrancee; thirdly, in payment of subsequent mortgages or encumbrances (if any) in the order of their priority; and the surplus (if any) shall be paid to the mortgagor or encumbrancer, as the case may be." Is the category "moneys which may then be due or owing to the mortgagee or encumbrancee" to be read as extending to the expense incurred by a mortgagee in making permanent improvements without the mortgagor's consent or acquiescence? It would appear necessary that it should be read as extending to such expenditure if it is consistent with the principles of the Act to allow it in a mortgagee's accounts where the mortgagor is redeeming the security. But, even if these sections do not affect the present question and the principles to be applied are the same as those which would be applicable if the mortgage were by way of transfer of the legal estate, I agree that, because of the permanent change made in the nature of the security, the magnitude of the expenditure in relation to the debt and the absence of consent or acquiescence on the mortgagor's part, it would not be reasonable to allow the expenditure in the mortgagee's accounts.

In my opinion, the appeal should be dismissed, but subject to the variation in the decree of the Supreme Court appearing in the order of this court.

Subject to a variation of the decree agreed upon by the parties by which the word "net" is inserted after the words "demolition of the said premises and of the" and before the words "rents and profits of the said premises," appeal dismissed with costs.

Solicitors for the appellant, *D. Lynton Williams, Ellis & Co.*
Solicitor for the respondent, *Glen Richards.*

J. B.

(1) (1855) 20 Beav., at pp. 643, 644 [52 E.R., at p. 752].