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ADSAN LAW

WHEN YOU FAIL TO PAY YOUR MORTGAGE INSTALMENTS

WHAT HAPPENS WHEN YOU FAIL TO PAY YOUR MORTGAGE INSTALMENTS?

Mortgages are part and parcel of life. Chances are that you will finance a purchase of property using a housing loan and the monies in your Central Provident Fund (“CPF”) Ordinary Account. This article discusses the practical aspects of an individual (“Alex”) failing to pay his mortgage instalments on time.

What is a mortgage?

A mortgage is a loan by the Bank (the “**Mortgagee**”) to Alex (the “**Mortgagor**”) to finance the purchase of a property (the “**Property**”). The Property is used as security for the loan and the Bank is known as a “**secured creditor**”. In exchange for the loan monies, the Bank is given several rights against the Property. This allows the Bank to hedge against the risk of Alex defaulting on the loan.

There are generally the following documents in relation to the mortgage (together, the “**Mortgage Documents**”):

- a. letter of offer (also known as a facility letter) – which sets out briefly the terms of the housing loan, such as duration of the mortgage, applicable interest rate and amount of monthly instalment;

- b. standard terms and conditions governing the mortgage;
- c. instrument of mortgage – which contains a description of the land, particulars of the mortgagor and mortgagee, prior encumbrances etc. Where the Property is still under development, there will be additional documents such as a Deed of Assignment and the mortgage will be signed in escrow;
- d. memorandum of mortgage – which contains the covenants and conditions, and is filed with the Singapore Land Authority.

What happens when Alex fails to pay his mortgage instalments?

Contractually, failure to pay is an event of default under the Mortgage Documents. This means that the Bank may terminate the mortgage. In such circumstances, the Bank is entitled to demand immediate payment of all the monies owed.

Letters of Demand and Notice to Quit

If Alex fails to pay his mortgage instalments, the Bank may give him an extension of time to pay the arrears. Alex may seek further indulgences from the Bank, such as a restructuring of the mortgage. Any indulgence granted would be at the absolute discretion of the Bank and without prejudice to the rights of the Bank.

If Alex remains unwilling or unable to pay, the Bank will terminate the mortgage. In the standard terms and conditions of most banks, it may also be provided that the Bank may terminate other banking facilities granted to Alex (eg, credit card facilities). Legal proceedings would not have commenced at this stage.

Generally, the Bank will notify the following parties in writing at least 1 month prior to commencing legal proceedings:

- a. Notice to Quit to the Mortgagor
When the Mortgagor defaults on his mortgage instalments, the Bank is statutorily entitled to enter into possession of the Property. To do so, the Bank must give at least one month's notice to the Mortgagor¹. This is called a "Notice to Quit".
- b. Notice to Quit to the Occupiers of the mortgaged property
The Bank will also inform the Occupiers of its intention to exercise its power of entry into possession of the Property, and request the Occupiers to deliver possession of the Property to the Bank (ie, hand the keys over to the Bank). This covers a situation where the Mortgagor has rented out the Property.

¹ Section 75 of the Land Titles Act.

c. Letter to the Housing & Development Board (“HDB”)

If the Property is a HDB flat, then the Bank will inform the HDB of the Mortgagor’s default.

d. Letter to CPF Board

Where CPF monies were used in the purchase of the Property, generally the Mortgagee Bank will have a first charge on the sale proceeds of the Property. This means that upon the sale of the Property, the sale proceeds must first be utilised to repay the Housing Loan and other expenses incidental to the sale before the balance sale proceeds (if any) are used to refund CPF monies (principal as well as accrued interest) utilised.

Commencing legal proceedings - mortgage action under Order 83 rule 5 of the Rules of Court

Upon being served the Notice to Quit, Alex can deliver vacant possession of the Property to the Bank. In the event that he does not do so, the Bank can commence legal proceedings by filing an Originating Summons under Order 83 of the Rules of Court. These proceedings are frequently referred to as “mortgage actions”.

Generally, the Bank will seek the following orders in the Originating Summons:

- a. that the Mortgagor and Occupiers of the mortgaged property deliver vacant possession of the mortgaged property;
- b. if there are furniture remaining in the mortgage property after the Bank has taken possession, that the Bank gives the Mortgagor not less than 7 days’ notice to remove the furniture;
- c. that the Mortgagor pays the outstanding sum together with interest and other fees (as provided for in the Mortgage Documents); and
- d. costs to be paid by the Mortgagor.

The Bank also files an affidavit in support of the Originating Summons to, *inter alia*²:

- explain the circumstances under which the right to possession arises and the state of the account between the parties;
- set out the particulars of every person who is in possession of the mortgaged property;
- include a notice endorsed on the outside fold of the affidavit informing the Mortgagor that the Bank intends to claim delivery of possession at the hearing; and
- exhibit a true copy of the mortgage.

If the Court finds in favour of the Bank, the Court will order that possession be given to the Bank usually with a stay in execution for a period of time – that is, the Court will give Alex a period of time to pay up the loan or move out before the Bank can take possession of the Property.

² Order 83 rules 2 and 3 of the Rules of Court.

Taking possession of the Property

If the Mortgagor or Occupier fails to deliver vacant possession to the Bank upon the expiry of the stay of execution period, the Bank may seek to enforce the judgment by applying to the Court for a writ of possession³.

A writ of possession is valid for 12 months beginning with the date of its issue⁴. It must be noted that the costs of the writ of possession, regardless of whether it was executed or unexecuted, shall be allowed against the Mortgagor, unless the Court orders otherwise⁵. The writ of possession will be executed by the Sheriff. Usually, this includes changing the door locks of the Property.

Upon taking possession of the Property, the Bank has a duty to exercise due diligence to put the Property to beneficial use. This means the following:

- if the Bank ought to rent out the Property but does not – the Bank has to account to Alex for the rent that he ought to have received⁶;
- if the Bank rents out the property – the Bank has to obtain rent that a person acting reasonably diligently would get for the property⁷;
- to exercise due diligence to rent out the Property if a sale does not take place within a reasonable time⁸.

What if the Property is tenanted – can the Bank evict the Tenant upon taking possession? It boils down to whether the Bank recognises the tenancy⁹. The Mortgage Documents usually provide that the Mortgagor cannot lease the property without the Mortgagee's consent. Consequently, where the prior consent of the Bank was not obtained, the Bank will not recognise any tenancy, and will likely seek to evict the Tenant.

Mortgagee sale

The Bank has a statutory right to sell the property. This right accrues when the mortgage money has become due¹⁰ – ie, when Alex fails to pay an instalment under the mortgage. It must be noted that although there are statutory pre-conditions before the right to sell can be exercised, these can be, and usually are, varied by the Mortgage Documents¹¹.

³ Order 45 rule 3 of the Rules of Court. The writ of possession must be in Form 85.

⁴ Order 46 rule 6 of the Rules of Court.

⁵ Order 46 rule 8 of the Rules of Court.

⁶ *Lee Nyet Kiong v Lee Nyet Yun Janet* [1997] 2 SLR 713.

⁷ *ibid.*

⁸ *Pte Ltd Motorcycle Industries (1973) Pte Ltd v Indian Overseas Bank* [1992] 2 SLR 453.

⁹ *Singapore Finance Ltd v Matterhorn (Pte) Ltd* [1989] 3 MLJ 193.

¹⁰ *Payne v Cardiff Rural Council* [1932] KB 241.

¹¹ Sections 24(2) and 25 Conveyancing and Law of Property Act.

In exercising this power of sale, the Bank is under a duty to act in good faith and to take reasonable steps to obtain the true market value or the best price reasonably obtainable at the date of sale of the Property¹². However, the Bank is not required to wait for market conditions to improve, or to delay a sale in the hope of obtaining a better price; but must ensure that the state of the Property does not deteriorate should the sale be postponed. It is also not necessary to sell the Property by auction, or for the sale to be advertised¹³. In the event that Alex is able to procure a buyer for the Property on his own, he must seek the Bank's consent to the sale price and terms.

The Mortgagor must note that the proceeds from the sale of property may not be as high as they expect. Deductible expenses include payment of agent and legal fees incurred in the sale. Should there be a shortfall (that is, if the proceeds of sale are insufficient to cover the outstanding sums under the mortgage, refund of CPF monies and deductible expenses), the Mortgagor remains liable for the shortfall.

As an illustration, suppose Alex purchases the Property at the price \$1,000,000.00. Alex finances this purchase in the following manner:-

Cash down-payment	: \$ 50,000.00
CPF down-payment	: \$ 50,000.00
Mortgage loan	: \$ 900,000.00 (monthly loan instalment: \$ 2,500.00)

Alex then uses his CPF funds to repay the monthly mortgage instalment payments to the Bank. He does not make any additional payments in cash.

- a. 2 years later, Alex's CPF monies utilised towards the monthly instalment payments towards the mortgage loan amount to \$60,000.00. Let's assume that interest on the mortgage loan adds up to \$22,500.00. The outstanding sum owed by Alex to the Bank is now \$862,500.00.
- b. Alex now defaults on his mortgage instalments. The Property was sold for \$800,000.00 in a mortgagee sale.
- c. Upon the sale of the Property, the principal amount of CPF monies utilised, together with the accrued interest, would have to be returned to Alex's CPF account – we assume this to be \$115,500.00. Further, there are agent fees, legal fees and other miscellaneous fees incurred in the sale – we assume this to be \$20,000.00.

¹² *How Seen Ghee v Development Bank of Singapore Ltd* [1994] 1 SLR 526, *Lee Nyet Kiong v Lee Nyet Yun Janet* [1997] 2 SLR 713.

¹³ *Goh Chin Soon v Vickers Capital* [2001] 1 SLR 728, *Motorcycle Industries (1973) Pte Ltd & Anor v Indian Overseas Bank* [1993] 2 SLR 1.

d. Hence, there is still a shortfall of \$198,000.00.

Sale price	\$ 800,000.00
<u>Less</u>	
Housing Loan	\$ 862,500.00
Expenses in relation to the sale	<u>\$20,000.00</u>
Shortfall amount	(\$ 82,500.00)

This means that Alex is liable to the bank for the balance amount of \$82,500.00. In addition, a request would have to be made to CPF Board to waive the requirement to refund the amount of \$115,500.00 that he had utilised from his CPF account.

Power to appoint Receiver

The Bank has a statutory power to appoint a receiver of the income of the Property¹⁴. This right accrues when the mortgage money has become due¹⁵. The Receiver manages the Property, such as renting out the Property, collecting and distributing rent.

The Receiver is considered an agent of the Mortgagor¹⁶, and owes several duties to the Mortgagor¹⁷:

- a. a duty of good faith;
- b. in exercising his powers of management, a duty to bring about a situation in which the debt (and interest thereon) can be repaid;
- c. a duty to manage the property with due diligence.

In practice, the Bank exercises its power to appoint a receiver instead of its power of sale only where renting out the Property is profoundly more beneficial than selling it.

Other consequences

The Bank may exercise its right to set-off

The Mortgage Documents usually allow the Bank to set off the outstanding arrears owed under the mortgage against the assets in the Mortgagor's other accounts with the Bank.

¹⁴ Section 24(1) Conveyancing and Law of Property Act.

¹⁵ *Payne v Cardiff Rural Council* [1932] KB 241.

¹⁶ Section 29(2) Conveyancing and Law of Property Act.

¹⁷ *Roberto Building Material v Oversea-Chinese Banking Corp* [2003] 3 SLR 217.

Suppose Alex has a savings account with the Bank – the Bank is contractually entitled to debit funds from Alex’s savings account to pay off the arrears owed under the Mortgage. Most bank’s terms and conditions will provide for this right regardless of whether the assets are singly held in Alex’s name or jointly with third parties.

Mortgagor’s death or bankruptcy

The Mortgage Documents usually include a clause which provides that the Mortgagor is obliged to pay the monies secured under the mortgage notwithstanding the Mortgagor’s death, bankruptcy, liquidation, receivership or judicial management (where applicable). Therefore, in the event that Alex passes away, the obligation to pay the outstanding mortgage falls on the estate.

As a secured creditor, the Bank’s rights will not be adversely impacted in the event that Alex is adjudged a bankrupt. This means that the Bank may continue to exercise its right to repossess and sell the Property. However, the Bank has to inform the Official Assignee or the Private Trustee in Bankruptcy (as the case may) within 30 days of the bankruptcy order of its intention to claim interest, and realise the security within 12 months of the bankruptcy order, failing which the Bank may not be able to claim further interest, unless an extension of time is granted by the Official Assignee or the Private Trustee in Bankruptcy¹⁸.



Author: Henry Lee

CONTACT

ADSAN LAW LLC
300 Beach Road Level 26
The Concourse
Singapore 199555
Tel: 68282828
www.adsanlaw.com

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¹⁸ Section 327(4) Insolvency, Restructuring and Dissolution Act 2018.