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The application of the equitable doctrine of consolidation:

AIB Mortgage Bank v O'Toole [2018] IECA 6

Background

The doctrine of consolidation generally applies where a borrower has mortgaged separate properties to secure separate debts owed to the same lender. Where a borrower has defaulted on one of those debts, the doctrine of consolidation allows the lender to pool the assets secured by the borrower and to realise those secured assets against the aggregate sum owing, rather than confining the lender to recovering only the secured assets securing the distressed loan.

The doctrine protects a lender's rights by preventing borrowers from selectively redeeming mortgages over valuable properties, thereby potentially leaving the lender at risk of assets of inadequate value supporting the outstanding debts while the Borrower has the benefit of a surplus. It would be inequitable for a borrower to redeem security supporting a performing loan only without discharging its obligations in respect of other distressed loans.

The right of consolidation is an equitable right. Accordingly there are a number of conditions that must be satisfied in order for a lender to exercise its rights of consolidation. These include:

1. the contracted date for redemption of the underlying loan must have passed;

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- 2. the mortgages in question must have been originally created by the same person; and
- 3. all applicable mortgages must be in existence at the time that consolidation is claimed.

Case summary

To date, the equitable doctrine of consolidation has been recognised by the Irish Courts in limited circumstances.

The decision of Ms. Justice Whelan, delivered on the 29th January, 2018 in <u>AIB Mortgage Bank v</u> <u>O'Toole & Anor</u> as part of the judgment considered the equitable doctrine of consolidation.

Allied Irish Banks, p.l.c. (the **Bank**) had advanced a number of loans to the appellants which were secured by mortgages containing terms which effectively cross secured the loans advanced by the Bank. The loans advanced are referred to in the following paragraphs as the **First Loan** and the **Second Loan** respectively.

In 2015, the appellants disposed of a property which, amongst others, was securing the First Loan. The Second Loan subsequently went into default. Having effected the sale of the property, one of the appellants proceeded to partially redeem the First Loan and retained the surplus proceeds of sale. The Bank obtained ex parte orders restraining disposition of the additional properties which were also securing the First Loan. The High Court directed that a preliminary issue be determined which was whether the Bank was entitled to rely upon the terms of the loan agreements and security instruments (the **Finance Documents**) to prevent the disposition of the remaining properties secured in favour of the Bank.

The appellants argued that the equitable doctrine of consolidation was engaged and unless the Bank had complied with the stringent requirements of that doctrine it was not entitled to purport to consolidate the First Loan and the Second Loan. The Bank disputed the appellants' contentions, noting that the Bank was not seeking to exercise the equitable doctrine of consolidation and that the terms of the Finance Documents were clear that the First Loan and the Second Loan were to be crossed secured. The Bank state that it was not relying on the doctrine of consolidation and that it had no application to the case.

In reaching judgment, Mr. Justice Binchy determined that the concepts of "secured monies" and "secured liabilities" as well as a covenant to pay all monies owing to the Bank in the Finance Documents for each loan were clear and unambiguous such that the High Court found in favour of the Bank.

The Court of Appeal Decision

The appellants appealed the decision of the High Court on a number of grounds including the ground that notwithstanding the express terms of the Finance Documents, the Bank was not entitled to rely on such terms for the purposes of enforcing cross security unless they could

demonstrate strict compliance with the equitable doctrine of consolidation in addition to the express terms of the documents.

In determining whether the provisions of the doctrine of consolidation could be implied into the Finance Documents, Ms. Justice Whelan concluded that it cannot be contended that the provisions of the doctrine are to be read into a security instrument in each case. Ms. Justice Whelan referred to the fact that the Bank at no point sought to exercise the doctrine of consolidation and that the Bank were relying solely on their contractual rights. She further clarified that there is no authority for the proposition that a lender can be compelled to exercise this right by an attempt of a borrower to unilaterally invoke the remedy. Rather, the doctrine is reserved for the benefit of the lender to be invoked at their will.

In upholding the High Court decision, Ms. Justice Whelan found that the language contained in the Finance Documents was sufficiently clear and unequivocal such that the terms expressly provide that the loans are effectively cross secured by the separate mortgages and the Bank had validly invoked the cross security arrangement. It was noted that all of the properties comprised as security in respect of the First Loan should remain as security in respect of the outstanding sums due on the Second Loan.

Conclusion

This decision reasserts the position that the right of consolidation belongs to a mortgagee and not to the mortgagor. It confirms that a mortgagor cannot compel a mortgagee to invoke or exercise consolidation. As with other equitable remedies, it is for the party who wishes to avail of an equitable remedy to invoke it.

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