

MORTGAGE AND CHARGE: A PRACTICAL OVERVIEW OF THE NEXUS BETWEEN THE TWO TERMINOLOGIES

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INTRODUCTION

When we discuss a term like Charge generally, we refer to an interest or maybe a right that a creditor acquires in an asset. This asset can be movable property like a cupboard, cell phone, fast moving consumer goods, furniture, etc. or it can also refer to immovable property like land, tree that is in a position to receive sustenance from the soil, that what is attached to the earth etc. Similarly, in general parlance when we talk about mortgage what a layman would understand would be that it is generally a legal title, which one would give to another in exchange for a benefit. However, this might not be entirely accurate. Let us see how the law defines these two terms.

According to *Practical Law, UK*, a charge is a security over an asset which gives the lender the right to have the particular asset and its proceeds of sale appropriated to the discharge of the debt in question. A charge does not transfer ownership; it is merely an encumbrance on the asset.¹ According to *Black's Law Dictionary*, a mortgage is an applied lawful lien by the mortgagor in exchange for obligation discharge or debt repayment.² Thus, we see how the legal definitions of Mortgage and Charge are very different from the terms used in general parlance. This is perhaps because with common usage in the English language, the words have been used with a wider interpretation than they actually contain.³ Having defined the terms in a legal

¹ *Practical Law, Practical Law UK Signon*, URL: <https://uk.practicallaw.thomsonreuters.com/2-107-5890?transitionType=Default&contextData=%28sc.Default%29&firstPage=true&bhcp=1>
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² *Black's Law Dictionary, The Law Dictionary*, URL: <https://thelawdictionary.org/legal-mortgage/>
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³ Chaplin, H. W. "The Story of Mortgage Law." *Harvard Law Review*, vol. 4, no. 1, 1890, pp. 1–14. JSTOR, www.jstor.org/stable/1321129.

sense let us now see what the *Transfer of Property Act, 1882* describes about mortgage and charge under Indian Law.

Section 100 of the Transfer of Property Act, 1882(henceforth referred as “the Act”) defines a charge.

“Where immovable property of one person is by act of parties or operation of law made security for the payment of money to another; and the transaction does not amount to a mortgage, the latter person is said to have a charge on the property; and all the provisions hereinbefore contained which apply to a simple mortgage shall, so far as may be, apply to such charge.”⁴

It says that where immovable property of one person is, by act of parties or operation of law, made security for the payment of money to another, and the transaction does not amount to mortgage, the latter person is said to have a charge on the property, and all the provisions hereinbefore contained which apply to simple mortgage shall, so far as may be, apply to such charge.⁵

“Nothing in this section applies to the charge of a trustee on the trust-property for expenses properly incurred in the execution of his trust, and, save as otherwise expressly provided by any law for the time being in force, no charge shall be enforced against any property in the hands of a person to whom such property has been transferred for consideration and without notice of the charge.”

Section 58 of the Transfer of Property Act defines what a mortgage is:

“A mortgage is the transfer of an interest in specific immovable property for the purpose of securing the payment of money advanced or to be advanced by way of loan, an existing or future debt, or the performance of an engagement which may give rise to a pecuniary liability. The transferor is called a mortgagor, the transferee a mortgagee; the principal money and

⁴ The Transfer (Amendment) of Property Act, 1882, No.4 of Parliament, 1882 (India)

⁵ Transfer of Property, *Law Teacher*, URL<https://www.lawteacher.net/free-law-essays/land-law/transfer-of-property-topic-critically-law-essays.php> Date Accessed : February 25, 2018

interest of which payment is secured for the time being are called the mortgage-money, and the instrument (if any) by which the transfer is effected is called a mortgage-deed."⁶

There are six types of mortgages. The types of Mortgages as described by the Transfer of Property Act, 1882 are:

- 1) Simple Mortgage
- 2) Mortgage by Conditional Sale
- 3) Usurfructory Mortgage
- 4) English Mortgage
- 5) Mortgage by Deposit of Title Deeds
- 6) Anomalous Mortgage

JUDICIAL INTERPRETATIONS

In *Re Bank of Credit and Commerce International SA (No.8)*⁷ Lord Hoffman attempted to provide a definition of charge and acknowledge that providing an exhaustive definition for the same was far from easy. He was happy with the description that a charge is a proprietary interest granted by way of security without a transfer of title or possession. He remarked that it is common for a charge to be an appropriation of an asset in discharge of a liability.

In *Carreras Rothmans v Freeman Mathews Treasure*⁸ the Hon'ble Peter Gibson J was of the opinion that a charge is created 'by an appropriation of specific property to the discharge of some debt or other obligation without there being any change in ownership either at law or in equity.

⁶ The Transfer of Property Act, 1882, *Supra Note 3*

⁷ [1998] AC 214 at 226

⁸ [1985] 1 Ch 207 at 227.

These two decisions can be interpreted to deduce two of the most essential elements of a charge.

They are;

- 1) The creditor obtains an equitable proprietary interest in the secured asset, but does not obtain either legal or beneficial title to it. Nor is it required that the creditor take possession of it.⁹
- 2) The creditor's interest is given to him by way of security for the discharge of a liability so that, when the liability has been discharged, the charge terminates.¹⁰

In *Govinda Chandra Pal vs Dwarka Nath Pal and Ors*¹¹ it was held that if an instrument is expressly stated to be a mortgage, and give the power of realization of the mortgage money by sale of mortgaged premises, it should be held to be a mortgage. The fact that necessary formalities of the due execution were wanting would not convert the mortgage into a charge. If, on the other hand, the instrument is not on the face to it a mortgage, but simply creates a lien, or directs the realization of money from a particular property without reference to sale, it creates a charge

In *Gopal vs Parsotam*¹² Justice Mahmood better explained the definition of mortgage ; “As understood in this country, mortgage cannot be defined better than what I laid down in the legislation of the Transfer of Property Act as this definition has not in any way altered the law but on the contrary has only formulated in clear language the notions of mortgage as all writers of the textbooks on Indian mortgages”. Every word of the definition is borne out of the decisions by Indian courts.

In *Stanley vs Wide*¹³, it was held by the learned Judge that A mortgage is conveyance of land or an assignment of chattels as security for the payment of debt or discharge of obligation for which it is give.

⁹ R. W. A. “Effect of Taking Possession of Mortgaged Property under a Chattel Mortgage as against a Junior Mortgagee.” Michigan Law Review, vol. 7, no. 7, 1909, pp. 580–583. JSTOR, JSTOR, www.jstor.org/stable/1273004.

¹⁰ Richard Calnan, *Taking Security*, Jordan Publishing UK, URL: <http://www.jordanpublishing.co.uk/practice-areas/commercial/publications/-taking-security-#.WpJz9naWbIU>
Date Accessed: February 26, 2018

¹¹ Gobinda Chandra Pal vs Dwarka Nath Pal And Ors, (1906) ILR 33 Cal 666

¹² (1883) ILR ALL 121 p 137

¹³ (1899) 2 Ch 474

In the case of *Raja Shri Shiva Prasad vs Beni Madhab*¹⁴ Justice Das said that “The broad distinction between a mortgage and a charge is that whereas a charge only gives the right of payment out of a particular fund or a particular property without transferring that fund or property, a mortgage gives the essence of a transfer of an interest in a specific immovable property. A mortgage being a jus in rem and a charge being a jus ad rem and the practical difference being that a mortgage is good against subsequent transferees and a charge is only good against subsequent transferees without notice.

Thus, we see from the above-cited cases and the excerpts of their judgements that from the very beginning as early as 1800s the common law judges viewed mortgage distinctly from that of charge. Even during colonial rule, the few judges who were of Indian nationality in the trial courts in India, supported this view, which is why in a legislation like the Transfer of Property Act, 1882 that came in to force as early as the 1880’s contains the essence of this distinction.

In fact even though several attempts have been made in the course of this research to find relevant cases pertaining to the distinction between mortgage and charge, but they are hard to come by perhaps because the judges of recent years assume the distinction to be a forgone conclusion and the detailed explanation as provided for in the precedents from the colonial rule and even after in the early 20th century clarify any existing doubts on the same.

KEY DIFFERENCES

1) Classification

In terms of classification of the two, from the definitions we saw that Mortgage simply put was an exchange of the legal title in return for a benefit, and Charge is the interest, which the creditor acquires in the property. Further we saw the how they were defined under the Transfer of Property Act, 1882.

¹⁴ (1922) ILR 1 Pat 387

Thus, from this we can infer that Charge is classified as being an interest, which the lender gets in a property. The Lender can acquire the same in three ways, A Mortgage, Pledge or a Hypothecation. Hence, Mortgage is essentially a method for the creditor to obtain a charge.

2) Creation of Right in REM

A mortgage is a transfer of an interest in specific immovable property but a charge is not. In a charge no right in rem is created, but the right is something more than a personal obligation, for it is a just ad rem, that is right of payment out of property specified, while a mortgage is a right in rem.¹⁵

A right in rem is a right against the whole world. In Charge, there is no transfer of right or interest in a specific immovable property whereas in mortgage there is. Charge is more of a just ad rem whereas mortgage is a right in rem.

3) By whom can it be created?

As we have seen earlier a Charge, can be created by an act of parties that is transfer intervivos or it can be done by the operation of law i.e. testamentary transfer. However, a Mortgage can only be created by the act of parties and creation by operation of law is rendered invalid.

4) Implied Existence of a Debt

In the case of a mortgage, whenever a mortgage is created, there is always most definitely an existence of a debt, which is implied. The same does not hold true for a charge however. In the case of a creation of charge there is not an implied an existence of debt, as laid down under Section 100 of the Transfer of Property Act, 1882.

5) Registration

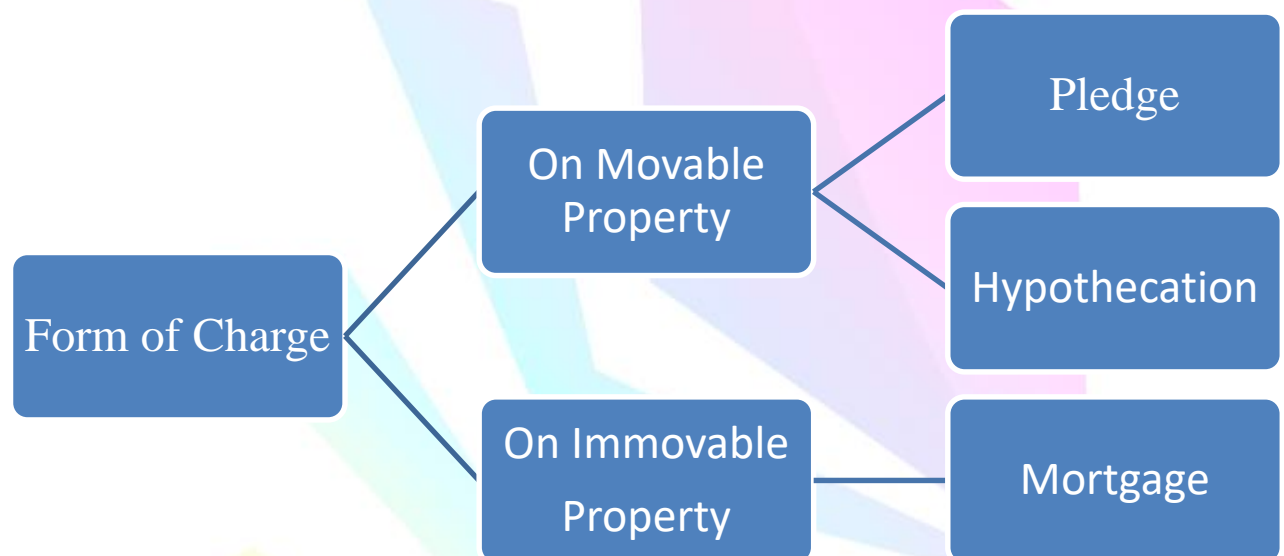
As we saw earlier, a Charge can be created by Act of Parties or it can be created by Operation of Law. In the case of a creation of charge by operation of law, it need not be registered. However, in creation of a mortgage, Section 59 of the Transfer of Property Act prescribes the

¹⁵ Transfer of Property, Law Teacher, URL<https://www.lawteacher.net/free-law-essays/land-law/transfer-of-property-topic-critically-law-essays.php> Date Accessed : February 25, 2018

registration of the Act of a Mortgage. Hence, all mortgages, regardless of their pecuniary value need to be registered.¹⁶

6) Notice

A mortgage is good against subsequent transferees and may be enforced against a bona fide purchaser for value with or without notice, while a charge is good only against subsequent transferee with notice.¹⁷ Hence a charge mandatorily requires notice in order for it to be good against a subsequent transferee but a mortgage in certain instances can be enforced without notice.



IMPORTANCE OF THE DISTINCTION

As seen in the earlier paragraphs, when the terms Mortgages and Charge are used in common parlance, quite often they are used interchangeably and there appears to be no clear distinction between the two. Over time, due to wider interpretation, the two have been used as synonyms and this has led to several instances, which highlight the importance of its distinction.

¹⁶ Sturges, Wesley A., and Samuel O. Clark. "Legal Theory and Real Property Mortgages." *The Yale Law Journal* 37, no. 6 (1928): 691-715. doi:10.2307/789669.

¹⁷ *Id. No.6*

In the first world war in the early 20th century, there was a lot of confusion as to the duties of the army and armed forces personnel. This was mainly due to the misinterpretation of the word Security that led to confusion as to whom it should be provided. There was law in effect at the time, which provided for different applications of the term security with respect to Mortgage and Charge.

In *London County & Westminster Bank v Tompkins*¹⁸, the Court of Appeal questioned this legislation and it was examined thoroughly. Due to the confusion over the difference between Mortgage and Charge, it led Scrutton LJ to come to a conclusion that although there was a difference between a mortgage and a charge, 'common law judges seem to use the terms with no particular distinction'.

In *Kennard v Futvoye*¹⁹: It was held in the words of the eminent Stuart VC that 'If there be a simple charge without an equity of redemption, that is, if there be nothing more than a debt charged upon an estate, without any conveyance of the estate to the creditor, or any right or equity of redemption reserved, such a security is not a mortgage ... because a charge is at once extinguished by payment of the debt, and from its nature must subsist till the debt is satisfied.' Furthermore, generally it is considered that Charge is an Equitable right whereas Mortgage is a Legal right. It is easier to enforce a legal right than it is to enforce an equitable right. Thus due to the cloud of confusion over Mortgage and Charge it is fairly easy for a person having a claim of a charge to convert it to that of a mortgage and enforce the claim as a claim of Mortgage. For example, consider the illustration given below.

Illustration: A transfers a property to B. B requires a particular benefit and thus mortgages it to X. Later X refuses to give the benefit as promised to B stating that it is already paid. B wishes to enforce his claim of mortgage against X in order to obtain his benefit. Knowing this, X declares that B doesn't have a claim of mortgage but that of a charge, taking advantage of the lack of clarity of distinction between the two. B finds it harder to enforce his equitable right.

Thus in the above instance we see another reason why the distinction between a charge and a mortgage is important.

¹⁸ [1918] 1 KB 515 at 528.

¹⁹ (1860) 2 Giff 81 at 92-93.

CONCLUSION

It is clear that Mortgage and Charge although similar have their innate differences. Even though they are quite often used interchangeably in common parlance, such a mistake cannot be afforded when they are described in a legal sense. With the help of the Transfer of Property Act, 1882 we have seen 6 key differences between the two with regards to their classification, registration, by whom they can be created, notice, implied existence of debt, creation of right in rem, etc.

The mortgage, pledge, and charge are forms of real security, which broaden the options of the creditor beyond reliance on the promise of the debtor to pay. The mode of security to be adopted depends on the parties and the dictates of circumstances. These legal terms are important in all business or contractual transactions amongst parties (be it companies, management and business ventures). There are municipal or domestic laws in various countries to regulate such transactions.²⁰

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