

Spotlight on Interest-only mortgages and options

A dark cloud looms on the horizon for many interest only mortgagors as the consequences of not having a 'repayment vehicle' in place to pay off the capital at the end of the term is beginning to hit 'home'. Our article discusses what a client can do where the term has ended or due to end.

Finally the mortgage is paid...Or is it?

Around 17% (1.67 million) of mortgages in the UK are either interest-only or part-capital repayment. There is genuine concern that many homeowners will face the prospect of becoming homeless as they will not have sufficient funds to settle the demand for payments made by banks in years to come.

Customers are responsible for ensuring that the mortgage is repaid in full at the end of the term. Engaging early in the life of the mortgage provides both lenders and customers more opportunity to agree affordable repayment plans.

So, as advisors what are the signs, what should borrowers do?

Your client only wants help making an offer of repayment to a creditor. The exploration finds that your client has several years left on their interest only mortgage term with nothing in place to repay the capital element.

Mortgage lenders have to follow the FCA Mortgages and Home Finance: Conduct of Business sourcebook (MCOB) rules in particular [MCOB 13 Arrears, payment shortfalls and reposessions](#). The rules can be useful to mention when trying to come to an arrangement with a lender. As well as treating the client fairly if they are in arrears, the rules say that a lender must have a written policy on how to deal with customers who are in arrears.

How long before your client retires? Would a repayment mortgage be an option? Do they have 15 years of working life left? See [MCOB 11 - Responsible lending](#), and responsible financing of home purchase plans. This is useful information for advisers to be aware of, as well as informing their clients that lenders are now duty bound to carry out affordability checks.

Is your client prepared to downsize or find alternative accommodation by using available equity in the current home? Selling the property may be the only realistic option.

Is your client in receipt of Support for Mortgage Interest (SMI) payments? Remember this benefit is being [replaced by a loan](#) from 5 April 2018. Options will need to be explored and discussed.

The Money Advice Service has [information for clients](#) who have interest only mortgages.

Your client comes to see you with a possession claim fuming stating that the mortgage has been settled. You politely inform them that even though the term has ended, the capital remains outstanding. What else can you tell them?

Delay possession

Your client could attend the hearing and request that possession be delayed for six months to allow for the sale of the property. It would be advisable to start the ball rolling as soon as

possible prior to the hearing so essentially the property is on the market by the hearing date. It would be advisable to take evidence of the sale to the hearing.

Suspend the possession

Your client could make an application to suspend the possession order using the provisions in [section 36 of the Administration of Justice Act 1970](#) and [section eight of the Administration of Justice Act 1973](#). Lenders' solicitors often try to limit the courts powers by saying that the borrower has to be able to pay the contractual instalment plus an amount towards the arrears every month which will clear the arrears before the end of the mortgage term, also known as the 'Norgan' rules.

In the Court of Appeal case of [Justin Oliver Zinda v Bank of Scotland Plc \[2011\] EWCA Civ 706](#) the judgment considers the powers under section 36 and section eight and finds them to be much wider than traditionally thought. The case was actually decided on a different issue (about whether consolidation of arrears discharges a possession order – it doesn't) but the Court of Appeal interpreted the powers to mean that possession can be suspended where the court is satisfied that the arrears and any instalments falling due will be paid by the end of the 'reasonable period', and this can include a period of no payments under the order, or a lump sum payment either right away or in the future. There is no requirement for the contractual instalments to be paid, a judge can interfere with the terms of the contract although they may be reluctant to do so.

Time order option

The statutory instrument that made time orders available for first mortgages and second charge mortgages is [article five of The Financial Services and Markets Act 2000 \(Consumer Credit\) \(Miscellaneous Provisions\) \(No.2\) Order 2014](#). It came into effect on 31/3/2014, so it would appear time orders for regulated mortgage contracts have been available since then.

Where the term has already expired, we believe applying for a time order is possible. The wording of [section 129 of the Consumer Credit Act 1974 \(CCA\)](#) does not limit the timeframe at all. It limits applications to certain circumstances (i.e. following default, during an enforcement action by the creditor etc.) but not to within the period of the agreement. Case law on time orders also support that the main consideration is that the making of an order is 'just' as per section 129.

So, although a time order could be a viable option for a client for the mortgage arrears, this is only likely to be the case once court action has been commenced. There is an untested argument that a time order application could be made following the issuing of the notices required by MCOB 13.4.1 and 13.4.5. This is based on the view that these notices are the equivalent to the required CCA notices and therefore have the same effect in having a time order has an option. These arguments are discussed by Robert Rosenberg in IMA's Quarterly Account, Issue 40, Spring 2016.

On the other hand, time orders may not be available in some circumstances. Where the balance of the interest only mortgage agreement was entered into before 1 October 2008 and the amount borrowed was over £25,000, then the agreement would not have been a regulated agreement. Therefore, for the purpose of a Time Order application the borrower will be unable to show there was a [Consumer Credit Act 1974](#) (CCA) regulated agreement.

Section 126(2) CCA states:

'Subject to [section 140A\(5\)](#) (unfair relationships between creditors and debtors), a regulated mortgage contract which would, but for [article 60C\(2\)](#) of the Regulated Activities Order (exempt agreements: exemption relating to the nature of the agreement), be a regulated

agreement is to be treated for the purposes of [Part 9](#) (judicial control) as if it were a regulated agreement.'

However, an interest only mortgage providing credit of £100,000 for example would have been exempt from the CCA for a reason other than the exemptions detailed in article 60C(2). It would have been exempt because it provided credit which exceeded the £25,000 limit.

So, it seems to follow that section 126(2) does not open time orders up to exempt agreements which were not regulated for reasons other than those listed in article article 60C(2).

If you have clients in similar circumstances, please contact us for further advice.