

Debt Farming?

Unfair treatment of mortgage
customers in arrears by
UK lenders

Govan Law Centre
Summary Report

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GOVAN
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CENTRE

[1] INTRODUCTION

The unfair treatment of mortgage customers in arrears by UK lenders is a socially important and far-reaching issue. Homeowners in financial difficulty struggling to keep their heads above water can be pushed under by lenders' unfair, repetitive or excessive administration charges. Almost manageable debts can become impossible to meet, as debts cycle disproportionately out of control due to a series of arrears, missed payment, management and other administrative charges added to the defaulting consumer's mortgage account.

In Govan Law Centre's experience mortgage arrears charges are all too often a form of 'rent extraction' whereby profit is extracted for the sake of it from vulnerable homeowners trying to avoid repossession and homelessness. We believe all too often the application of such charges can represent a form of monthly '*debt farming*' in the UK by some mortgage lenders.

Several sub-prime lenders have already been fined by the City regulator, the Financial Services Authority (FSA), for failing to treat mortgage customers in arrears fairly. In October 2009, GMAC-RFC was fined £2.8m, while in July last year Redstone Mortgages Ltd were fined £0.63m for poor treatment of mortgage customers in arrears.¹ In April 2010, the Kensington Mortgage Company Ltd was fined £1.22m for the unfair treatment of its customers in arrears.²

DB Mortgages, part of the Deutsche Bank Group, was fined £0.84m in February this year by the FSA for its unfair treatment of mortgage customers in arrears, including repetitive and/or excessive charges.³ In September this year, Swift 1st Limited were fined £630,000 for unfair treatment of some customers in arrears of their mortgage, which included applying excessive charges that did not reflect a reasonable estimate of the cost of administering mortgage accounts in arrears.⁴

In January 2010, the FSA set out its proposals to toughen up its approach to how UK lenders treated customers in arrears of their mortgage, with CP10/2: '*Mortgage Market Review: Arrears and approved Persons*'.⁵ This consultation led to a Final Policy Statement document from the FSA in June 2010, together with changes to the Mortgage and Home Finance: Conduct of Business sourcebook (MCOB).⁶ Changes included making it clear that lenders should not apply charges to customers in arrears who were adhering to a payment arrangement.

However, prior to the June 2010 changes to MCOB, it was always the case that lenders should not impose administrative charges to customers in mortgage arrears unless those charges were '*a reasonable estimate of the cost of additional administration required as a result of the customer being in arrears*'. This rule is found in MCOB 12.4.1(1):

"12.4.1(1) A firm must ensure that any regulated mortgage contract that it enters into does not impose, and cannot be used to impose, a charge for arrears on a customer except where that charge is a reasonable estimate of the cost of the additional administration required as a result of the customer being in arrears."

In other words, it has always been clear from the FSA's Rules that charges in mortgage arrears cases should be fair and necessary, and restricted to the actual cost of extra necessary administrative work

¹ <http://www.fsa.gov.uk/pages/Library/Communication/PR/2009/147.shtml>; and

<http://www.fsa.gov.uk/pages/Library/Communication/PR/2010/120.shtml>

² <http://www.fsa.gov.uk/pages/Library/Communication/PR/2010/065.shtml>

³ <http://www.fsa.gov.uk/pages/Library/Communication/PR/2011/025.shtml>

⁴ <http://www.fsa.gov.uk/pages/Library/Communication/PR/2011/079.shtml>

⁵ http://www.fsa.gov.uk/pages/Library/Policy/CP/2010/10_02.shtml

⁶ http://www.fsa.gov.uk/pubs/policy/ps10_09.pdf

(as opposed to providing a means to generate a mark-up or extra profit stream for lenders). For example, in the Kensington Mortgage case the FSA identified failings relating to unfair charges, and excessive charges, whereas in the GMAC-RFC case failings included excessive charges which did not reflect actual administrative cost. In the Redstone case, exception was taken to sending 'repetitive, excessive and confusing correspondence', and the unnecessary use of litigation.

Accordingly, while MCOB 12.4.1(1) is concerned with the imposition of excessive charges which do not reflect actual administrative costs, the use of the expression '**additional administration required as a result of the customer being in arrears**' in the Rule makes it clear that the lender is not at liberty to set up systems that generate additional administration for the purpose of rent extraction, as opposed to necessary and meaningful administrative work. In other words, repetitive and unnecessary charges are not permissible.

The issue of interest to Govan Law Centre (GLC), as a charitable, free legal resource, defending many hundreds of repossession actions across the West Coast of Scotland each year, is whether lenders have changed their unfair practices towards mortgage customers in arrears? Has poor practice improved since sub-prime lenders were fined by the FSA? Have lenders begun to treat mortgage customers more fairly since the FSA's June 2010 Policy Statement on this issue?

In order to test this hypothesis, GLC undertook a random sample and analysis of 24 repossession actions from its case work, with an emphasis on sub-prime lenders, who have generally had the worst track record in this area. Key findings are set out below in Section 2.

[2] KEY FINDINGS

- (1) **Lenders are continuing to treat mortgage customers in arrears unfairly.**
 - Sub-prime lenders continue to be the worst offenders imposing multiple charges most of which are unnecessary and excessive (see for example case 3 below, Preferred Mortgage Ltd can levy all of these monthly charges: unpaid direct debit fee £30, arrears fees £45, telemessage fee £25, questionnaire fee £75, referral to solicitors £50, repossession fee £29.38, litigation management fee £115, late payment fee £25; Southern Pacific Loans Ltd (case 2), Rooftop Mortgages Ltd (case 9), Central Trust plc (case 11), and other sub-primes are equally poor).

- (2) **Kensington Mortgage Company Ltd continued to impose unfair charges despite being fined by the FSA in April 2010**

See case 22.

- (3) **High Street lenders are also treating customers in arrears unfairly**
 - For example, the Bank of Scotland and Halifax impose monthly missed payment fees of £35 and arrears management fees of £35 (cases 13 and 23), while Santander plc charge £40 per month as an arrears fee (case 16); consider that the monthly default charge for credit card missed payments is generally £12, and it cannot be the case that these charges reflect the banks' actual administrative costs per individual customer.

- (4) **The total amount of administrative arrears charges (excluding legal fees) from the 24 sample cases was £19,593 or an average per case sum of £816. 20% of the sample study were required to pay administrative arrears charges over £2,000.**
- (5) **The total amount of administrative charges for defaulting active UK 'sub-prime' mortgage customers in arrears may be roughly estimated at £200m.**⁷ (100,000 households). That compares to a rough estimate of £178m of administrative charges for defaulting active mortgage customers with 'prime' High Street mortgages in the UK (218,000 households).⁸

[3] GLC OBSERVATIONS AND MAIN RECOMMENDATIONS

Sub-prime lenders and prime lenders

In our experience, sub-prime mortgage customers suffer the highest level of unfair administrative charges, and are generally the least able of customers who can afford to pay such charges. Unnecessary, unfair, repetitive or excessive charges compound the financial difficulties of such customers.

Given that so many arrears charges appear to be contrary to MCOB 12.4.1(1) (and separately, under the Unfair Terms in Consumer Contract Regulations 1999), Govan Law Centre believes the FSA should consider requiring all 'sub-prime' lenders to undertake a review of their active mortgage accounts with a view to voluntarily reimbursing all of their customers who have been charged unnecessary, unfair, repetitive or excessive charges.

Refunds could be credited to the mortgage account (thus reducing the level of consumer mortgage arrears).

We believe a similar review exercise should also be considered for High Street 'prime' mortgage lenders. Such a retrospective review has recently occurred with the mass misselling of Payment Protection Insurance (PPI) by UK banks and financial intermediaries, and there appears to be no good reason why such an approach could be considered with the mass imposition of unnecessary, unfair and excessive mortgage arrears administrative charges in the UK.

What represents a fair mortgage arrears charge?

A few years ago credit card lenders generally charged £25 to £30 per month or more as a standard default charge where a customer failed to make his or her minimum monthly payment. When in 2006 the Office of Fair Trading (OFT) advised credit card companies it would take enforcement action where credit card charges exceeded £12, by and large the industry reduced its charges to £12.⁹

⁷ There are 400,000 such sub-prime active mortgages in the UK, with 25% with arrears of 90 days or more; taking an average figure of £2,000 in charges, produces an estimate of £200m (excluding closed accounts): see: <http://www.ft.com/cms/s/0/616755c4-2d68-11e0-a4bf-00144feab49a.html#axzz1Rnsb0xKw>

⁸ Based on 10.9m prime first charge mortgage customers in the UK with a 90 days or more default rate at 2%; taking an average figure of £816 in charges, produces an estimate of £178m (excluding closed accounts): see: <http://www.cml.org.uk/cml/media/press/2914>

⁹<http://www.offt.gov.uk/news-and-updates/press/2006/68-06>

We believe it is both unnecessary and unfair to impose a series of monthly charges where a customer is in mortgage arrears; no purpose is served other than creating an additional income stream for lenders. In particular, there is no meaningful purpose or customer service gained by imposing routine monthly charges, given that where customers are subjected to legal proceedings they will have to pay the substantial legal costs of their lender in any event. Accordingly, even where a sub-prime lender attempts to argue that it costs 'x pounds' per administrative activity and that 'x pound' is a reasonable estimate of their costs, it is generally the case that most of these activities are repetitive, and unnecessary from an independent viewpoint.

Further, if credit card companies can undertake monthly default 'management' for £12, there is little reason that a lender cannot do likewise, under the proviso that we do not accept such activity serves any meaningful purpose each month, prior to either enforcement action or a repayment plan being set up.

ABOUT THIS SUMMARY REPORT

This summary report was written by Mike Dailly, GLC's Principal Solicitor; case work sampling and analysis was undertaken by Christine McKellar and Laura Simpson, GLC trainee solicitors, with the assistance of law student volunteers from Glasgow University's School of Law.

ABOUT GOVAN LAW CENTRE

Govan Law Centre (GLC) is a registered Scottish charity (SCO30193). It uses the law to tackle disadvantage and poverty. It is a community controlled law centre with its own solicitors and caseworkers. GLC specialises in meeting unmet legal needs in housing, homelessness, debt, discrimination, education, employment, and more generally in welfare law. GLC uses its knowledge and skill to influence decision makers and social policy at all levels and campaign for law and social policy reform for the benefit of the people it serves. It employs around 24 full-time staff in offices in Glasgow's Govan, and Govanhill. For more information about GLC please see:

<http://govanlc.blogspot.com> <http://www.govanhilllc.com> <http://www.edlaw.org.uk>

[4] CASE BY CASE ANALYSIS (RANDOM SAMPLE: 24 REPOSSESSION ACTIONS)

Case	Lender	Case Status	Charges Applied	Historical and /or Continuing
1. (CM)	GE Money Home Lending	Dismissed	Missing Installment Fees (£30) Unpaid Direct Debit Fees (£25) Calling In Notice (£50) Instruction to Solicitor (£100) Total - £ 310	Account from 16 May 2007 up until 09 April 2010 – not known whether continuing as case dismissed
2. (CM)	Southern Pacific Loans Ltd	Sisted (December 2010)	Arrears Counsellor Fee (£100) Arrears Management	Account from 01 July 2007 up until 01 November 2010 – not known whether they

			Fees (£50) Litigation Fee (£100) Litigation Management Fees (£115) Late Payment Management Fee (£25) Debt Counsellor Fee (£86.25) Total - <u>£2076.25</u>	continued to be added following case being sisted
3. (HM)	Preferred Mortgages Limited	Dismissed (January 2011)	Unpaid Direct Debit Fees (£30) Arrears Fees (£45) Telemessage Fees (£25) Final Reminder/Default Notice Fee (£25) Second Charge Questionnaire Fee (£75) Referral to Solicitors Fee (£50) Repossession Fee (£29.38) Litigation Management Fee (£115) Late Payment Management Fee (£25) Total - <u>£1539.38</u>	Account from 07 August 2004 up until 04 November 2010 – unknown whether client continues to receive such fees
4. (SJK)	Southern Pacific Mortgage Ltd	Consented to decree (superceded extract until September for MTR)	Late Payment Fees (£25) Late Payment Fees (£50) Late Payment Fees (£115) Total - <u>£2460</u>	Account from 01 December 2006 up until July 2010 – not known whether continued to be charged these while Mortgage to Rent going through
5. (SJK)	Abbey National Plc	Dismissed	Mortgage Arrears Fees (£35) Mortgage Arrears Fees (£40) Fee for Litigation Instruction (£265.50) Total - <u>£680.50</u>	Account from 26 September 2007 up until 01 November 2010 – not known whether continuing, although client is currently meeting payments
6. (LS)	Platform Funding Ltd	Sisted (April 2011)	Late Payment Fee (£40) Formal Notice (£25)	Account covers 3months!! April to June 2010 – likely that charges continued to be

			Sols Instructed (£80) Total - £225 (for period in statement – likely to be more)	added until case sisted
7. (SJK)	Preferred Mortgages Limited	Case active. Case called on 24 th June 2011 and it was requested that case be continued for 6 weeks.	No account available; however, copy of a letter from Lender dated 15 th January 2011 stating that while the account remains in arrears the clients will be charged one of the following fees, in any particular month depending on their arrears status: <ul style="list-style-type: none"> • Late payment management fee £25 • Arrears management fee: £85.00 • Litigation management fee £115 • Field agent Fee: £94 	No account available
8. (LP)	GE Money Home Lending	Sisted (motion to recall recently put in by lenders)	Only have account from 31/01/11 to 30/04/11, but charged £128 in this period, for Admin fees and Debt Counseling. Also given “A guide to our fees” which shows the amounts charged as standard.	Account only up until 30/04/11, although client has advised that he is still being charged
9. (LP)	Rooftop Mortgages Ltd	Dismissed, been re-raised	Monthly arrears fees (£75) Unpaid direct debit fees (£30) Counsellor visit fees (£130) Solicitor instruction fees (£100) Monthly arrears fees (£50) Total of £2100	Account only from September 2007 up until 01 February 2010, but likely that client still being charged

10. JL	Your Mortgages Plc	Sisted (motion to recall sist recently lodged by lenders)	Letter advising that arrears monitoring charge of £54 would be added for the month, but not shown on account. Likely to be monthly charge hidden in payment.	Unknown
11. JL	Central Trust Plc	Sisted for Mortgage to Rent	Collection costs (£50) Unpaid cheque (£150) Collection costs (£60) Total of £2030 Also has letter with "Tariff of Fees and Charges" which shows e.g. Solicitors Instruction Fee of £100 and Issue of Default Notice £50	Account from 31 August 2006 to 10 August 2010, although likely that still being charged while Mortgage to Rent going through
12. JL	Nemo Personal Finance	Sisted 10/11/10 for Mortgage to Rent application	Unpaid direct debits (21 x £30) £630 Unpaid cheque fees (2 x £30) £60 Default notice £50 TOTAL £740	20/11/06 – 05/08/10 Unknown whether any further charges have been applied.
13. JL	Halifax (client has handed this account in with account above)	No details of any legal action taken by this lender in respect of arrears	Missed payment fees (4 x £35) £140 Arrears letters / call fees (6 x £35) £210 Arrears management (5 x £35) £175 TOTAL £525	15/12/08 – 23/11/09
14. JL	Southern Pacific Personal Loans Ltd	Dismissed (<i>Wilson</i>) 09/03/11 Loan term has now ended & calling-up notice likely to follow	Unpaid direct debit £25 (02/10/07) Administration Fee £50 (05/08/08) Arrears management (£60 + £60 + £85) £205 Litigation management (17 x £115) £1,955 Late payment fee £25 Late stage arrears management fee £95 TOTAL £2,355	Unpaid d/d 02/10/07 Admin fee 05/08/08 All other charges made between 09/06/09 and 13/04/11, and are likely to have continued to date.

15. JL	Bank of Scotland	Decree granted 11/05/11	Arrears management fees (3 x £35) £105	12/01/10 – 31/12/10 Likely to have continued to May 2011
16. JL	Santander UK plc	No legal action taken by this lender	Mortgage arrears fee £40	On 11/12/10
17. JL	Swift First Ltd	Mortgage to rent application successful	Arrears charge (2 x £23) £46 Admin fee (2 x £33) £66 Default charge £250 Management charges (9 x £70 + 5 x £35) £805 Letter sent 2/6/09 £100 <u>TOTAL £1,267</u>	12/06/08 – 28/09/09 probably continued until November 2010
18. JL	Platform Funding Ltd	Decree granted 26/01/11	Formal notice charges £25 Late payment fees (28 x £40) £1,120 “Lit. Pack” charges £80 <u>TOTAL £1,225</u>	3/5/07 – 2/8/10 likely to have continued
19. JL	Preferred Mortgages Ltd	Arrears cleared April 2011	No statement on file – only relevant info is a letter from lender dated 09/08/10 setting out arrears charges for account	09/08/10 – April 2011
20. JL	The Mortgage Business Plc	Previously dismissed (<i>Wilson</i>), calling-up notice issued 10/05/11	Arrears management fees (4 x £35) £140	27/07/09 – 20/08/09
21. JL	Paratus (Formerly GMAC)	Case continued for investigations,	Arrears fee £50 (31/05/11)	05/05/11 – 31/05/11

		last hearing 29/6/11.	TOTAL £50 Summary only, no detailed statement on file – awaiting this from pursuer.	
22. JL	<u>Kensington Mortgage Company Ltd</u> <u>Fined in 12th April 2010- £1,225,000</u>	Previously dismissed (<i>Wilson</i>). No further action yet, client paying arrears.	Monthly arrears charges of £50 and other various charges ranging from £20- £30. Total £680	Have continued to apply charges after being fined in April 2010. Account from 1st Sept 2009- 1st Nov 2010
23. JL	Bank of Scotland Plc	Previously dismissed (<i>Wilson</i>), calling-up notice issued 08/02/11. Awaiting further details from client.	Missed payment fees (10 x £35) £350 Arrears Management Fees (7 x £35) £245 Field Agent Costs £85 Instruct solicitors £125 TOTAL <u>£805</u>	10/06/09 – 25/08/10 probably continued after this date
24. JL	GMAC – RFC	Hearing 13/07/11, MTR failed, repossession likely	Arrears fee £50 Total- £59	On 31/10/10 Likely to be more charges