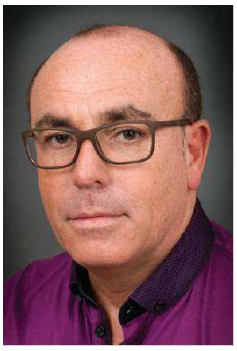
Mortgage contracts

After Alexander: money lending and group actions - Part 1

Post *Alexander (as representative of the 'Property118 Action Group') v West Bromwich Mortgage Company Ltd*, **David Bowden** discusses what is next for mortgage lending and group actions.



About the author
David Bowden is a solicitoradvocate of David Bowden Law®.

The appeal court's ruling

The Court of Appeal allowed the action group's appeal ([2016] EWCA Civ 496). It held that a mortgage lender could not increase its rates on its tracker mortgages other than by reference to the Bank of England base rate. The lender had encountered liquidity problems, and sought to plug the gap by trying to increase rate margins on tracker mortgages where customers had three or more buy to let mortgages. As a result, the lender has had to pay compensation of £27½m to affected customers.

What was the dispute in this case?

A lender took a decision to increase rates on its tracker mortgages. These mortgages had a rate of 1.99% over the Bank of England base rate. The lender decided to add an additional 2% per year premium to this rate for customers who had three or more buy to let mortgages with the lender. The customers formed a representative action group named 'Property118', and brought a court claim seeking a declaration about this rate rise. This split into two issues:

- Was clause 5 of the lender's standard mortgage terms (which did mention the right to vary interest rates in this way) a term of the mortgage contract or was the contract, instead, governed by the lender's mortgage offer (which did not mention the right to vary interest rates in this way)?
- Did the first bullet point of condition 14 of the lender's standard mortgage conditions allow the lender to require borrowers to repay the loan on one month's notice even though the borrower was not in breach of the loan and had made all payments promptly?

How did this action group come to be assembled?

In September 2013, over 6,000 buy to let mortgage borrowers received a letter from West Bromwich Mortgage Company advising them that an additional premium was being added to their tracker mortgages. This letter also threatened to call in the mortgages with just 30 days' notice if the lender deemed them unprofitable. Mark Alexander received one of these letters. He initially posted an article on the Property118.com website (which he had launched and which has around 200,000 members). His article ranked highly in 'Google News' as well, so many other borrowers in the same situation who shared his outrage also found out about Property118 Action Group when searching online.

How was the action group's claim funded?

As at March 2014, over £450,000 was raised by action group members to fight the case through the judicial process. To fund the action, affected borrowers who had a mortgage with West Bromwich had to pay £240 to join the action group (plus a contribution to a marketing campaign). This fee was payable for each loan, so someone with five buy to let mortgage would have to pay £1200. One member said that the rate increase would have cost him £35,000 over the full mortgage term, and the proposed fee seemed to represent good value for money.

Although the action group obtained a quotation for after-the-event insurance to cover the lender's costs if it lost the case, it felt that the premium quoted was too high. In the end, Cotswolds Barristers (a specialist chambers that represented the action group on a direct access basis) opened an escrow account with BARCO and deposited sufficient funds to cover the lender's estimated costs for the hearing and the appeal. Any payments out of this account had to be signed off by both Mark Alexander and Mark Smith, head of chambers at Cotswold Barristers. This arrangement satisfied the lender's solicitors that the account represented adequate security for its costs.

How were decisions made by the action group?

Mark Alexander said that decisions in relation to the litigation were made by a small steering group that he chaired and which was advised by Mark Smith. Cotswold Barristers represented the action group in the Commercial Court and in the appeal court. The action group had a secure forum created for and accessible only to its paid-up members.

What happened in the Commercial Court?

In January 2015, Mr Justice Teare ruled that the lender was not prevented from increasing its rates in this way ([2015] EWHC 135 (Comm)). He dismissed the challenge from Property118 Action Group. An application for permission to appeal that ruling was granted in May 2015.

What happened at the Court of Appeal hearing?

The appeal was heard by Sir Brian Leveson, president of the Queen's Bench Division, Sharp LJ and Hamblen LJ. There was a string of interventions and hostile questions by Raymond

Cox QC for the lender. Michael Ashcroft QC, for the borrower, produced an extract from the latest edition of Emmet and Farrand on Title, which said that the decision of Teare J was wrong.

What did the Court of Appeal decide?

The court unanimously allowed the appeal. It ruled that clause 5 was inconsistent with the lender's offer documentation, which referred to the product as being a tracker mortgage. Hamblen LJ said that a lender has a right to require repayment if there is a breach or a default event, and if there are other circumstances where a lender could call in the loan then it should have been set out in the offer document.

What has been the reaction to this judgment?

The lender announced that it would not seek permission to appeal this case to the Supreme Court. Since then, the Bank of Ireland and the Skipton

Building Society have admitted that their standard mortgage documentation is drafted in a similar manner.

Fiona Hayles, a partner in the Cheltenham oÿce of Harrison Clark Rickerbys, says that her primary reaction was surprise that the Court of Appeal had taken such a robustly consumerist approach in circumstances where these were all buy-to-let borrowers with substantial property portfolios. She notes too that these borrowers probably had the benefit of professional advice on what they were entering into. She labels this 'another example of the rather paternalistic approach that we have seen recently'. She says that it has been the approach followed by the courts in payment protection insurance or fiduciary relationship cases but, interestingly, not in the interest rate hedging products cases.

Malcolm Waters QC, the leading barrister specialising in retail banking and mortgages, of Radcliffe Chambers in Lincoln's Inn says that:

While not coming as any great surprise, the Court of Appeal's decision has certainly highlighted the risk to lenders in relying on generally worded terms in their standard mortgage conditions to override specially agreed terms which form part of the description of the mortgage product in the offer document. The risk here is not that the language of the general terms will be found too narrow to cover what the lender has done. The risk is that, precisely because the general terms are wide enough to allow the lender to do what it has done, and thereby defeat the main object of the contract (the provision of the product described in the special terms), the general terms will be found inconsistent with the special terms, with the result that they do not form part of the contract at all.

What should lenders do now?

Those who are drafting or reviewing mortgage documentation for lenders will, in the light of this judgment, need to consider this carefully. The Court of Appeal said that it was not helped in its task by considering screen dumps from the lender's website about whether these products were or were not tracker mortgages. The court approached its interpretation task in a narrow way by comparing the lender's standard mortgage conditions with the offer letter sent to the customer. It was, however, assisted in deciding what was meant by a 'tracker mortgage' by considering the definition of this term set out in Retail mortgages: law, regulation and procedure.* What is very clear is that there should be consistency in all the lending documentation, be it in the terms and conditions, mortgage deed or offer letter and in the advertising or marketing material, be it conventional print or an electronic format.

Russell Kelsall, a partner in the London office of TLT Solicitor's financial services regulation team, says:

The Court of Appeal's decision is causing mortgage lenders to look at their terms and conditions, and consider the extent, if any, that they have terms which conflict with the terms of the mortgage offer. The problem is arguably more acute where mortgage lenders have entered into mortgage contracts with consumers when the issue of fairness under the Unfair Terms in Consumer Contracts Regulations 1999 [SI No 2083] and, for contracts on or after 1 October 2015, the Consumer Rights Act [CRA] 2015 apply.

Malcolm Waters QC agrees that lenders will clearly need to ensure that if they are contemplating a change to a feature of the mortgage product described in the offer, they have the necessary power to make the change under the contract. He says:

The lesson from Alexander is that any such power will need to be presented to the borrower as qualifying or modifying the description of the product. That is unlikely to be possible unless the power is clearly incorporated into the description of the mortgage in the offer document. If the borrower is a consumer, great care will also be needed to avoid the power being found unfair (and so not binding on the borrower) under Part 2 of the [CRA] 2015.

*** Malcolm Waters QC, Elizabeth Ovey and Mark Fell, Sweet & Maxwell, 2013**