

Court of Appeal considers whether a bank should bear losses from fraudulent 'sale & rent back' scheme

Dispute Resolution analysis: David Bowden, freelance independent consultant, notes the submissions made to the Court of Appeal in *Mortgage Express v Lambert* and considers the implications of this case for financial services practitioners.

Original news

Mortgage Express Limited v Lambert

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Court of Appeal, Civil Division (Lewison, Gloster LJ & Cobb J)

The Court of Appeal has heard submissions and reserved judgment in this case. A home owner in financial difficulties sold her home at an undervalue and was allowed to stay there under a lease. The transaction was presented to the lender as a sale. When the lender found out what had really happened, the home owner claimed an over-riding interest. Should the loss suffered be laid at the door of the lender or not? HHJ Simpkins in the Dartford County & Family Court gave judgment for the claimant lender on 15 July 2015. The defendant borrower appealed against this ruling to the Court of Appeal.

What is the significance of this case?

Last year the Supreme Court handed down its judgment in *Southern Pacific Mortgages Ltd v Scott (North East Property Buyers Litigation)* [2015] 1 All ER 277 ('*Scott*'). This case also concerned a 'sale and rent back' scheme. However despite this judgement, this issue has not gone away because the way all the schemes are set up varies. Here there was a bridging loan which was not secured by mortgage which the homeowner's lawyers said made a difference to *Scott*.

For what was previously decided on 'sale & rent back' schemes see previous LexisPSL® news piece: *Priority and the indivisible transaction after Scott v Southern Pacific*

What are the facts?

Mrs Lambert owned a property worth about £120,000. She had a mortgage with Blemain Finance for about £26,000. Mrs Lambert was in a poor financial position. Blemain obtained a possession order. Mrs Lambert was desperate not to become homeless. Mrs Lambert obtained a 2 week bridging loan to pay off her mortgage with Blemain. Mrs Lambert then purported to sell her home to 2 men called Sinclair and Clements. Mortgage Express agreed to provide a mortgage to Sinclair and Clements. Mortgage Express was concerned that the property was being sold at an undervalue. It required an insurance policy to be taken out in case at a later date there was a bankruptcy and a trustee sought to set aside the sale as being one at an undervalue.

The sale completed and Mrs Lambert remained in her home. Sinclair and Clements had granted Mrs Lambert a 90 year lease. Mrs Lambert failed to pay her monthly 'rent' of £250 and Sinclair and Clements failed to pay anything to the lender. The lender discovered the true position and brought an action to recover possession of the property. Mortgage Express also got into financial difficulty,

was bailed out by the UK taxpayer and its book of mortgages is now administered by UK Asset Resolution.

What ruling did HHJ Simpkins give?

On 15 July 2015 Judge Simpkins upheld the claim and gave judgment for the lender in its possession action.

What were the issues the Court of Appeal was asked to address?

The grounds of appeal were on 3 interlinked bases:

- The lender was on notice that something was suspicious about this transaction because of the sale at a gross undervalue. It should have investigated and failed to do so.
- Mrs Lambert's interest as a person in actual occupation was not over reached by the mortgage and sale to Sinclair and Clements. Mrs Lambert retains an overriding interest in the property.
- The conveyancing solicitors who dealt with this should have protected Mrs Lambert's interests by registering a restriction at HM Land Registry.

What does the appellant borrower say?

The appellant says that Judge Simpkins came to the wrong result. She says there is a key difference to *Scott* because there the 'sale and rent back' scheme arrangers organized a 'buy to let' mortgage with a lender which **directly** discharged the home owner's existing mortgage. In *Scott* the homeowner was granted an assured shorthold tenancy. Here, Mrs Lambert took out an unsecured bridging loan to pay off Blemain. There was a gap of 14 days whilst this bridging loan was in place before completion of the Mortgage Express mortgage.

Mortgage Express knew this was a transaction at an undervalue – the purchase price was £30k and its own conservative valuation was £120k – and this put them on notice to make enquiries. Mrs Lambert says that Mortgage Express cannot blow hot and cold – on the one hand requiring an insurance policy to cover it in case of a 'transaction at an undervalue to defeat creditors' claim in any future insolvency – and then at the same time maintain it did not think there was anything suspicious here. Finally, Mrs Lambert's counsel said she was put under a 'spell' from the scheme arrangers and that the court should exercise any equitable jurisdiction applicable in her favour.

Are there any prior authorities on this?

For more detail on the authorities cited in the hearing, see: *The case law behind Mortgage Express Limited v Lambert*.

What does the claimant lender say?

The lender says the position is clearly dealt with by the LPA 1925 and the Supreme Court decision in *Scott*. It says all Mrs Lambert had was an equitable interest in the property. This was over reached when the mortgage with Mortgage Express completed. Mrs Lambert has no answer to the possession claim. It says her only remedies lie with:

- Sinclair and Clement for misrepresentation, and/or

- The conveyancing solicitors for failing to protect her interest by lodging a restriction or inhibition against her title at HM Land Registry.

The lender says that the existence of these remedies against these people are irrelevant to its claim for possession. For more detail on the property legislation that applies, see: *The statutes relied on in Mortgage Express Limited v Lambert*.

What interventions did the judges make? What points seem to be troubling them?

Lord Justice Lewison interjected the lender's counsel (Miss Nicole Sandells) to say that Mrs Lambert's interest was capable of being over reached. Lewison LJ wanted to know what would be the position where trustees acted in breach of trust. Lewison LJ queried what finding Judge Simpkins had made about what notice the lender had been put on but the lender's counsel submitted this was irrelevant to over-reaching. Lewison LJ observed that the judge's finding on *Etridge* had not been appealed.

Both Lewison and Gloster LJ queried the costs position. The lender's counsel said if it succeeded it would not seek an order for costs but rather simply seek to add them to the mortgage debt.

Lady Justice Gloster wanted to look at this through a prism of unjust enrichment. She queried why Mrs Lambert shouldn't be made to pay Mortgage Express on a subrogated basis at the interest rate charged by Blemain because she had been unjustly enriched. Gloster LJ looked at the property legislation and correctly noted that where there were 2 trustees for sale the position was slightly different and questioned whether the underlying assumption that 2 people were less likely to be dishonest than 1 was correct. Gloster LJ queried whether an allegation of fraudulent assistance by Mrs Lambert had any impact on the result. Gloster LJ was sceptical about the lender's claims that it hadn't realized the transaction was suspicious observing it was '*sharp enough to know it needed*' the insolvency insurance policy.

What lessons can financial services practitioners learn from this case?

We will have to see what the judgment says. Clearly the Supreme Court decision in *Scott* has not provided such comprehensive guidance on these sale and rent back schemes. There may be more litigation that appears where those advising home owners who have been duped looking for bright line distinctions from the *Scott* decision to avoid homelessness.

What should lawyers do next?

At the end of the hearing Lord Justice Lewison said the court would reserve its judgement. A draft judgment will be circulated in due course for any typographical errors to be corrected but this was not to be treated as an opportunity to re-argue the case. Lewison LJ gave no indication as to when judgment will appear but in view of the complexity of the legal argument seems it is more likely to appear the other side of the summer 2016 recess.

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