

Housing Rights

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Policy Response

The fair treatment of mortgage customers in payment shortfall: impact of automatic capitalisations

January 2017

when everyone has a **home**

Introduction

Housing Rights is the leading provider of specialist housing advice in Northern Ireland. We provide advice, support and representation to our clients, supporting them to deal with their housing issues and sustain their homes.

Since 2009, Housing Rights has offered a Mortgage Debt Advice Service for homeowners in Northern Ireland: as part of this service, Housing Rights solicitors can offer representation in court possession proceedings.

In 2014, Housing Rights represented 3 clients in mortgage arrears, in test cases before the Northern Ireland High Court. Our solicitors and advisers demonstrated that the lender, Bank of Scotland, had been capitalising our clients' arrears without their consent, resulting in higher Contractual Monthly Instalments; and simultaneously using the arrears as grounds to seek possession of the property.¹ The Chancery Master hearing the case characterised the Bank's practices as 'double-billing', and described these practices as 'unconscionable.'²

¹ See <http://www.housingrights.org.uk/news/bank-scotland-held-account>

² See <http://www.bailii.org/nie/cases/NIHC/Master/2014/11.html>

Summary

- Housing Rights welcomes the draft framework, which characterises lenders' practices as "automatic capitalisation" and aims to provide lenders with a structure which lenders can use to remediate affected customers.
- The Northern Irish housing market is distinctive in nature, when compared to the rest of the United Kingdom. Housing Rights would welcome further information on the FCA's analysis of the issues, and if this included a Northern Ireland-specific sample or consideration of any potential regional impacts, specific to Northern Ireland.
- Housing Rights welcomes the framework's recommendations relating to possessions and possession orders. We recommend that an explicit provision is added requiring lenders, where a mortgage subject to possession before Court is reconstituted, to inform the Court of the outcome of this, before continuing with possession action.
- Housing Rights feels that the option of "extinguishing arrears" should be available for affected clients.
- Housing Rights recommends that the framework include a provision that where a borrower has been meeting a higher, automatically capitalised monthly payment, and finds themselves potentially subject to possession for arrears due to any "reconstitution", the lender must consider offering "extinguishing of arrears" and formal, consensual capitalisation.
- Housing Rights does not support the "£10 threshold", as this could mean customers with substantial additional payments miss out on reconstitution.
- Housing Rights feels that, complexity notwithstanding, lenders should be responsible for remedying inaccuracies on customers' Credit Reference Agency records as fully as they possibly can.
- In the experience of Housing Rights advisers, clients in mortgage arrears will often take on debt from alternative sources to maintain their mortgage payments. Such customers, whose mortgages were wrongly increased, should have a right to compensation for consequential loss. This should be specified in the framework.
- In Housing Rights' experience, clients placed in a mortgage arrears situation often experience a significant amount of distress and inconvenience. Clients affected by automatic capitalisation were caused this distress with no legitimate basis. Therefore, Housing Rights would finally recommend that the FCA consider including provision in the framework relating to compensation for distress and inconvenience.

Housing Rights welcomes draft framework

Housing Rights broadly welcomes the Financial Conduct Authority's response to this issue, which aims to provide a framework which lenders can use to ensure 'fair remediation for customers.'³ We welcome the FCA's characterisation of lenders' practices as 'automatic capitalisation', leading to customers making overpayments, and the recognition that this may have led to unfair customer outcomes.⁴ Housing Rights also welcomes the FCA's statement that they 'expect firms to put this right, and ensure the practice ceases.'⁵

Housing Rights is pleased to offer several further comments on particular aspects of the proposed guidance framework, with the aim of ensuring that the framework fully provides fair remediation for affected customers.

Distinctive Northern Irish housing market

Housing Rights welcomes the FCA's steps to analyse the issues under consideration through conducting cross-firm analysis; convening an industry working group; and directly reviewing a sample of affected customers' mortgage accounts.⁶

As a housing advice charity operating solely in Northern Ireland, Housing Rights is conscious of the distinctive nature of the Northern Irish housing market when compared to the rest of the United Kingdom. Whilst house prices in Great Britain have generally recovered and/or surpassed their pre-crash levels, Northern Irish prices have fallen from a pre-crash peak of £225,000 to £124,000, as of October 2016.⁷ This has led to a significant proportion of Northern Irish borrowers being in negative equity, and having increased difficulties maintaining their mortgage commitments.⁸

Housing Rights would therefore welcome any further information on the FCA's analysis of the issues, and if this included a Northern Ireland-specific sample or consideration of any potential regional impacts, specific to Northern Ireland.

³ Financial Conduct Authority (2016) 'GC16/6 – The fair treatment of mortgage customers in payment shortfall: impact of automatic capitalisations', p7

⁴ Ibid., p3

⁵ Ibid., p4

⁶ Ibid.

⁷ See Fig. 3,

<https://www.ons.gov.uk/economy/inflationandpriceindices/bulletins/housepriceindex/oct2016#house-price-index-by-uk-country>

⁸ See Housing Repossessions Taskforce (2014) 'Initial Evidence Paper: Negative Equity, Arrears and Possessions in Northern Ireland' [Department for Social Development](#)

Possessions and possession orders

The FCA's proposed framework suggests that certain mortgage possession cases should be considered for remediation. The framework suggests that possession cases be considered where 'under the reconstituted view of the mortgage account, the customer would not have triggered the firm's possession processes [at that time]⁹ – that is to say, where if automatic capitalisation had not occurred, possession action would not have been commenced.

Where a possession order has been granted but not exercised, and the mortgage account meets the above description, the framework established that firms should consider:

- Applying to the court to have the Possession Order set aside;
- Flagging the case to ensure that if an application is made to enforce the Possession Order, the court is made aware of the reconstituted mortgage¹⁰

Housing Rights welcomes this element of the framework. In 2014, as discussed above, Housing Rights became aware of the issues addressed by the proposed framework precisely through discovering that possession actions were being undertaken on the basis of mortgage accounts which had been (incorrectly) automatically capitalised.

Housing Rights notes, however, that the above places no requirement on lenders in a scenario where possession action has been instigated and is before the Courts, but no possession order has been granted – for example, where possession action has been supported by an affidavit, which relies upon a mortgage account which has been automatically capitalised.

Housing Rights would therefore recommend that the framework also include a provision requiring lenders, where a mortgage account subject to possession action before a Court is reconstituted, to inform the Court of the outcome of this reconstitution before continuing with possession action.

⁹ Ibid., p11

¹⁰ Ibid.

The options of “reconstitution” or “extinguishing arrears”

The framework of remediation is based on the premise that the harm to customers, from automatic capitalisation, came from ‘the Contractual Monthly Instalment being higher than it would otherwise have been.’¹¹ The framework therefore proposes only to allow “reconstitution” – putting the mortgage back to what it would have been if the automatic capitalisation had never happened; and not the “extinguishing of arrears” – which is to say, reducing the arrears to £0 and *formally* and *consensually* capitalising these arrears.

Housing Rights would make 2 points in relation to this proposal:

- The FCA states that its case analysis found that the extinguishing arrears approach ‘would only be appropriate in a relatively small number of cases.’¹²

Firstly, Housing Rights feels it would be helpful to understand what a ‘relatively small number’ of cases actually is, as (for instance) a percentage of all affected mortgage accounts.

Secondly, Housing Rights advisers can attest that for some clients, “extinguishing arrears” may be the best option. The FCA indicate that ‘firms told [the FCA] that their systems could not cope’ with considering both reconstitution and extinguishing of arrears. It would be helpful if the evidence for this could be detailed. **Even if only a small number of customers would avail of the option of extinguishing arrears, Housing Rights feels that this option should be available, given the significant positive impact this could have for these customers.**

- **Reconstitution alone, in a small number of cases, could result in some customers becoming more vulnerable to possession action.**

For example, consider a borrower who has accrued arrears, and has begun to consistently pay off these arrears in the form of an automatically capitalised, and higher, Contractual Monthly Instalment (CMI).

Currently, this borrower is “on track” to pay off their mortgage and arrears by the end of the mortgage term. However, if they are subject to reconstitution as per the framework, they could find themselves with a lower monthly payment, but a legitimate sum of arrears which their lender could then use as grounds to begin possession action.

¹¹ Ibid., p10

¹² Ibid., pp10-11

Housing Rights recommends that the FCA framework include a provision that where a borrower has been meeting the higher, automatically capitalised CMI, and finds themselves potentially subject to possession for arrears due to any reconstitution, the lender considers offering the extinguishing of arrears and – formal, consensual – capitalisation.

Contractual Monthly Instalment: Increase Threshold

The framework proposes that firms will only reconstitute mortgage accounts where ‘at least one automatic capitalisation resulted in an additional payment greater than £10 per month.’¹³ The FCA states that when considering this issue with an industry working group, they considered a number of thresholds both higher and lower than £10, and found that a lower threshold would require ‘significant numbers of mortgage accounts to be reconstituted by firms where this would deliver little benefit to the customer.’¹⁴ No quantitative detail is given as to how ‘little benefit’ is defined.

Due to the potential for customers with substantial additional payments to “miss out” on reconstitution, and the lack of detail as to what the FCA have defined as ‘little benefit’, Housing Rights does not support the £10 threshold. Housing Rights would also ask the FCA to provide further information as to how they have defined ‘little benefit to the customer’ in the consultation paper.

In the experience of Housing Rights’ advisers, what the FCA define as a ‘low’ additional payment – anything up to £10 per month – could still have a significant effect on Housing Rights’ clients. For example, automatic capitalisation resulting in an additional payment of £9.50 per month, added as a result of the lender’s error, and paid for 5 years, would result in the customer making additional payments of £570. This is a substantial sum – particularly to clients in mortgage arrears, who often find themselves in that situation due to financial issues relating to (for example) loss of earnings and/or family breakdown.

¹³ Ibid., p9

¹⁴ Ibid., p10

Customers' Credit Reference Agency Records

The framework proposes that where reconstitution shows the customer has exited arrears sooner than originally recorded by the lender, firms should update customers' credit records to accurately reflect this. It does not propose to amend credit records for any other 'smaller' amendments, as the FCA 'understand[s] this is unlikely to provide much benefit to the customer', and has been informed that 'the process of correcting customers' credit files in volume is unprecedented and complex.'¹⁵

Housing Rights does not accept these considerations. The firms in question have made a significant error, which has had impacts on a significant number of mortgage customers across the United Kingdom; **complexity notwithstanding, it should be the firms' responsibility to remedy the effects of this error on customers, as fully as they possibly can.**

Consequential loss

The framework does not anticipate that firms will consider compensation for consequential loss – such as other debts incurred as a consequence of meeting the incorrect and higher Contractual Monthly Instalment – as 'when conducting [the] case analysis . . . [the FCA] saw limited evidence of consequential losses', and such compensation would 'require significant investigation in each case', meaning this was 'unlikely to be proportionate or practical.'¹⁶

Whilst Housing Rights acknowledges the potential need for significant investigation of individual cases for consequent loss compensation, we do not accept this as a consideration against including provisions concerning consequential loss.

In the experience of Housing Rights' advisers, clients in mortgage arrears will often take on debt from alternative sources, such as payday lenders, friends or family members, in order to maintain their mortgage payments. If these mortgage payments were wrongly increased, such customers should have a right to compensation for any consequential loss, and this should be specified in the framework.

¹⁵ Ibid., p12

¹⁶ Ibid.

Distress and inconvenience compensation

Despite “distress and inconvenience compensation” being stated in the title of paragraph 3.24 – along with consequential loss – it is notable that there is no substantive mention of distress and inconvenience compensation in the text itself.

In the experience of Housing Rights’ advisers, clients placed in an arrears situation – with associated communications, and the ultimate threat of possession of their homes – often experience a significant amount of distress and inconvenience.

Clients who are caused this distress and inconvenience as a result of automatic capitalisation – an error made exclusively by the systems of the lender(s) – were caused this distress and inconvenience with no legitimate basis. Whilst remediation may fix the technical error of automatic capitalisation, this will do nothing to acknowledge or compensate for the significant distress and inconvenience, wrongly caused to affected customers.

Housing Rights would therefore recommend that the FCA consider amending the framework, to include some provision of substance relating to compensation for distress and inconvenience.

For more information on this policy response, contact our Policy & Public Affairs Officer,
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