



Mortgages Made Easy Revision Notes

Written by
Adetomi Omidiora
MBA, CeMAP

UNIT 3

Mortgage Law, Policy, Practice and Markets

Contract

- Legal agreement between two parties
- Offer and acceptance
- Consideration Given (e.g buyer gives money and seller gives property).
- Intention to create legal relationship.

- Be entered into by persons who have the legal capacity to act within the clearly stated roles.

Requirements for entering into a contract

- 18 and above
- Sound mind
- Utmost good faith

Financial Regulations

Certificate in Mortgage
Advice and Practice
(CeMAP)
Module 2

Law of Agency

- An agent acts on behalf of another person (principal)
- It is important that an agent should be able to conclude contracts on behalf of principal.
- There must be a written contract
- The principal is liable for agent's actions but agent should only act within the remit as given by the principal.

Apparent Authority – Agent acts outside his remit

Ratification – Principal agreeing that agent's action was acceptable even after he has acted outside his apparent authority.

- Estate Agents act as Agents for sellers.

Borrowing

Types of Borrowers

Personal Borrowers (Individuals)

- Multiple of gross income used to determine how much they could borrow for mortgage purposes.
- When 2 people go into a *Joint tenancy* arrangement they are jointly and severally liable for the loan.

Partnership

- Partners jointly own assets and liabilities.

- Profits and losses are divided among partners
- Lender looks at partnership and assesses the risk.
- Lender looks at the financial standing of the partners themselves.
- Lender looks at Partnership Deed (agreement) to see what provisions are made for death, bankruptcy, and ability to borrow.
- Lender must look at partnership now and as an on going basis.

Corporate Borrowers (Companies)

- Loans to companies for residential and commercial purposes
- Loan assessed in terms of security offered and the borrower's ability to pay
Memorandum and Articles of Association – Company's powers to borrow
Articles of Association – Authority of its officers to borrow
Audited Accounts - The Company's status as a credit risk
Limited Liability – Personal Guarantees from the directors
- Loans to companies represent higher margins.
- Building societies are under obligation by law to limit corporate borrowing on land to a maximum of 25% of their commercial assets.
- 75% of Building society loans must be secured on residential properties.

Commercial Borrowing

- Individual or company seeks mortgage where security for loan is on commercial property.
- Lender considers borrower's status and viability of lending proposition; track record in running business, business plans, and expected impact of buying property.

Personal Representatives

- If deceased died testate (left a will) the personal representative is called an executor and he applies for a Grant of Probate.
- If deceased died intestate (no will) the personal representative applies for Letters of administration.
- Lenders can lend if the loan sought is in pursuit of managing the estate.

Attorneys

- Person creating the power of Attorney is the Donor.
- The Attorney is the Donee
- Lenders can lend to donees if the power of attorney document is current (not expired) and the document does not exclude borrowing on behalf of donor. *Enduring Power of Attorney (EPA)*

- An individual who expects to be mentally handicapped (might run in the family) chooses someone to represent him when this eventually happens.
- An EPA must be registered with the Public Guardianship Office
- An EPA can be created or revoked by the court of protection.
- In October 2007 (mentally capacity act 2005), EPAs were replaced by LPAs (lasting power of attorney)
- LPAs will cover financial affairs as well as welfare and personal affairs.
- LPAs must be registered with the office of public guardian.
- LPAs and EPAs can borrow but the document must empower them to do so.
- The document must also state the circumstances under which they can borrow.

Who Cannot Borrow

- Minors – Under 18s
- Undischarged bankrupts - for 12 months during which they can only borrow nominal amounts. After 12 months they are discharged and can borrow for mortgage purposes but are required by law to declare their former bankruptcy on mortgage application forms.
- Mentally handicapped – See EPA and LPA below.
- Individual Voluntary Arrangements (IVA) – Lenders are usually reluctant to lend, but arrangement does not prevent a person from taking out a mortgage

Trustees

- Appointed by Document (trust deed) to hold assets on behalf of others (beneficiary).
- Must be empowered by terms of deed to borrow.

Voluntary Housing Sector (non profit)

- Mortgages for housing associations are usually granted by taking security over the land that is being developed.
- A Registered social landlord (RSL) is qualified for government grants that can be used to develop housing. They can also borrow for mortgage purposes (rental and purchase) if they are empowered to do so.

Clubs and Associations

- Lender will check rules by looking at the constitution.
- Must also confirm authority of its officers to borrow.
- Ability to repay loan from accounts.

Mortgage

- Arrangement where an asset is used as security for a loan.

- Mortgagor – Borrower
- Mortgagee - lender
- FSA took over '*Regulation of Mortgage Contracts*' on 31st October 2004.

Two Types

Mortgage by Demise -Transfer of property from the lender to the seller on completion of the loan, and to borrower on full repayment of the loan (can only be arranged on unregistered property).

Mortgage by way of Legal Charge – Deed that states asset is charged with a debt.

Regulated Mortgage Contract

- Contracts entered to before 31/10/2004
- Lender provides credit to individual or trustee
- Loan must be secured on first legal mortgage on Land
- Property must be in the UK
- Borrower or close relative must use at least 40% of property.
- The FSA does not regulate second charges and corporate mortgages.

Conveyance

- Means of transferring rights in property.

Second and Subsequent Mortgages

- Occurs when a borrower has raised money once, against a property; and then raises additional money (second mortgage) against the same property with another lender.
- The priority of Mortgages is usually determined by the date of registration.
- A second mortgage is usually with a different lender because the lender of the original Mortgage will usually have a deed of further advance attached to the original mortgage.
- Mortgages are registered in terms of registration date on the property.
- Lender will only accept to do a second mortgage if there is sufficient equity.
- The interest rate for a second mortgage is usually higher than the first mortgage on the property because it involves a higher risk.

Deed of Postponement

- To set aside a second mortgage the original lender requires a *Deed of Postponement, which must be executed.*

- The Deed of postponement makes it possible to add a subsequent mortgage to an original one.

Two types of ownership

- *Joint Tenancy*- Each tenant owns whole of property. When a tenant dies property is automatically passed on to the surviving tenant irrespective of conditions laid down in the will.
- *Tenancy in Common*- Each tenant is responsible for his own share of the property.

Home Purchase Plan

- Islamic Mortgages
- Provider (e.g Bank) buys an interest in land and sells it to the home purchaser who is obliged to purchase it during or at the end of the specified period.
- It is required that the buyer, beneficiaries of a trust or related person occupies 40% of the dwelling.

Home Reversion Plan

- Subject to revised MCOB rules from 6/4/2007
- Provider buys all or part of the property from individual or trustee
- No interest is charged, as it is a transfer of legal ownership to the provider.
- Owner, related person or trust beneficiary is required to occupy 40% of land.
- Right to occupy the property can only be terminated if the occupier moves to a residential home, death of occupier, or end of a pre specified period of 20 years from date of original contract
- Provides more cash than Home income schemes, because property is passed to provider at death and only poor property growth can affect his interest.

Home Income Plan – Life time Mortgages

- Regulated by the FSA
- Mortgage advisor must take additional examination to advise on this.
- Enable elderly owners who do not have any mortgage on their property to release equity.
- Value of loan depends on value of house and age of applicant.
(Guide is 15 –20% of property value for a 60 year old to 50% for a 75 year old)

- Basically the older you are the more you will be allowed to borrow on the value of your house.
- No Capital or interest is paid during the Mortgage.
- Interest can be rolled up and be paid along with *original* loan when property is sold.
- Property can only be sold on death of borrower, Borrower moving to another property or residential home, or choosing to repay the debt.
- If the loan is used to purchase an investment plan (annuity), usually, the interest is not rolled up but is paid on a monthly basis out of the income from the plan (advantage here is that the debt is not increasing it is reducing, however annuity rates are low).
- Regulated by SHIP code of Practice (Safe Home income plans)
SHIP Code
- Applicant must be asked to seek independent legal advice.
- The lender must fund negative Equity that may arise.
- Borrower must be allowed to stay in his home for the rest of his life.
- Plan must be portable; borrower must be allowed to transfer the loan to another property.

Draw down Life time Mortgages

- Maximum limit agreed by lender, and borrower draws on these funds as needed.
- It is a good arrangement as interest is only charged on amount borrowed.
- Interest is rolled up rather than paid monthly.

MCOB Sourcebook

MCOB1 – Application and purpose

MCOB2- Conduct of Business Standards

MCOB3- Financial Promotions

MCOB4- Advising and selling Standards

MCOB5- Pre-application Disclosure (KFI)

MCOB6- Disclosure at offer stage

MCOB7- Disclosure at start of contract and after sale

MCOB8&9-Life time Mortgages

MCOB10- Annual percentage Rate

MCOB11- Responsible Lending

MCOB12- Charges

MCOB13 –Arrears and Repossessions

Land Tenure

- Denotes the way in which property title to land is held

- Law of Property 1925 states the two ways property can be held, Leasehold or Freehold.

Freehold Possession

- Estate in fee, absolute in possession
- *Fee* – right of property to be inherited when owner dies.
- *Absolute*- ownership has no limits or conditions.
- *Possession*- immediate entitlement to land where there are no previous claims.

Factors that can affect freeholder's rights

- National and Local planning legislation
- Covenants and Easements
- Local authority legislations
- Former Public utilities
- Passer bys
- Freehold title is not necessarily better than leasehold title in fact lenders do not like to consider Mortgages of freehold flats because of the difficulties associated with common areas (e.g one person's ceiling is another person's floor)

Leasehold Possession

- The Freeholder (lessor) agrees to lease land /property to someone else (lessee) who pays a ground rent for the lease.
- Term of years absolute.
- *Term* – Lease for specified period
- *Absolute* – ownership of lease is unconditional as it can be passed down to heirs.
- *Head Lease* – Created through this formal agreement. (states the term of lease, price of ground rent, and rights/obligations to leaseholder).
- Possible to create a *sub lease* with less term than original lease.
- For lending purposes lease must have 30 to 40 years before expiry.
- When lease expires land reverts back to freeholder.

Forfeiture

- Failure to comply with the terms of a lease could lead to termination of the lease, so it is the lender's rights, as stated in the legal charge, to fulfil these conditions if the borrower fails to do so.
- Lenders can also take out insurance policies to protect them against forfeiture.

Common hold /Leasehold Reform 2002

- Made it easier for leaseholders to collectively buy the freehold of their buildings.
- This Act also made it easier for individuals to extend leases. Leases can be bought after 2 years (of holding a long lease), for an additional 90 years from the end of the existing lease.
- Restrictive provisions of the past prevented many leaseholders from exercising the *Right of Enfranchisement*
- Freeholder is able to create lease for any time, however, a lease created for more than 21 years may gain statutory rights to buy the freehold.

Buying the Freehold of a Flat

- Must be a *Qualifying Tenant* – original lease must be for more than 21 years qualifying tenants can purchase leases where:
- 2/3rds of the flats must be on long leases (21 years or more)
- 1/2 of the freeholders in block must participate. (in a building with 12 flats, 9 of the flats must be on long leases and 6 leaseholders must agree to participate).
- There are 2 or more flats in the building.
- Internal floor area of the building used for commercial purposes excluding common areas (stairs, hallways) is not more than 25%
- Leaseholders, who do not want to participate, are not forced to be involved, they can lease from the new freeholders.

The following leaseholders cannot be qualifying tenants:

- Lease for commercial purposes
- Qualifying leaseholder owns more than 2 flats in the building.
- Charitable Housing Trust land.

Leaseholders cannot purchase if

- If it is a converted building with four or fewer flats, same person held freehold before conversion, and he or close relative lived in the flat as main residence in previous 12 months.
- Flat has been sublet by leaseholder on long lease
- 25% or more of the building's internal floor area is for commercial use.

Common hold Association

- Each owner owns freehold of property and share of the Common hold.
- Common areas in property owned by the association.

- Larger development called *Multi Unit Property*, individual property called *Unit*
- Land /Property is registered as an estate in common hold land at the Land Registry after association is formed.
- The association collects a common hold assessment, which is the similar to a management charge on a leasehold property.
- Common hold association must have a memorandum; articles of association and a common hold statement.
- All the Leaseholders and the Freeholder must be in agreement for the conversion.

The Following Factors Trigger Land Registration in the UK/Wales

- Land transfer after 1990
- Creation of first legal mortgage after 1/4/98
- Where a lease exceeding 7 years is granted. Application must occur within 2 months of transfer otherwise legal transfer is void. In this instance title reverts to previous owner who will hold it in trust for new owner.

HM Land Registry - Three Registers

The Property Register –details of the land, beneficial easements, title number of land and plan of property.

The Proprietorship Register – Name and address of estate or owner, property restrictions on ownership, nature of title and date of registration.

Absolute Title – Clear Title (could be good freehold title or leasehold title over 21 years)

Good Title - Leasehold title must be above 7 years. Here the leaseholder's title is good but the lessor's (freeholder) right to grant the lease is not guaranteed.

Qualified Title – Defective Title as registered.

Possessory Title - Usually in place when property's deeds are missing, and buyer wishes to raise money against good title. When it is held for 12 years right to land can be claimed but it can only be converted into absolute title after 15 years (squatter's rights).

Land Charges Register – Register rights over unregistered land.

- ***Puisine Mortgages*** – which are legal mortgages not protected by title deeds such as second charges.
- ***Matrimonial Interest*** – Spouse's interest, Family Law Act 1996 – updated to include civil partners.
- Anyone over the age of 17 who will not be a part of the Mortgage should be required to fill out consent to mortgage form by the lender to prevent an *overriding interest*.

Overriding Interest – Rights established in favour of a person who lives in a Property who is not a party to the mortgage, but never the less has an interest in it.

- Rights are established under S.70 of the Land Registration Act 1925 to prevent hardship and unfairness on non-owing spouse.

Consent to Mortgage Form

Any non-owing spouse who will not become party to Mortgage and all individuals over 17 living in the property must sign this form to prevent an overriding interest.

If in the future it comes to light that there are occupants in the property over 17 who have not signed this form, the lender should proceed with care not to prejudice its security.

Unregistered Land

- Rights on unregistered land can be registered through the Land Charges Registry.
- Difficult to establish good title when unregistered land is sold therefore a search must be conducted as far back as 15 years to establish anything that can affect the owner's rights (root title).

Class C land charges – registration for Puisine mortgages, which are mortgages not protected by deposit of the title deeds, for example second charges.

Class F land charges – registration of spouse's interests under provisions of Family Law Act of 1996.

Property Defects

Structural Movement – can be caused by poor construction on property or by subsidence on site.

Two types:

- 1) Long standing and Non- progressive – does not affect the lending decision
- 2) Recent and Progressive – Affects Lending. A structural engineer is invited for further investigations.

Other Issues

- Subsidence – land below the property drops unevenly causing property to shift. (e.g London Clay)
- Heave – Underground forces (e.g as a result of mining) causes property to rise unevenly.

Easements

- Right one person enjoys over land of another (e.g light, way, ventilation)
- Run with the land
- Two plots must be close together.
- Easements can be positive or negative (e.g right of way is an invasion of privacy for one party but necessary for the other party) *Dominant Tenement* – land that enjoys the right over another site.
Servient Tenement - land over which the right is held.
- The court can remove rights of way.
- Easements cannot usually impose a positive burden on the other owner except in instances where the other owner is asked to fence the land.

Covenants

- Run with the land and between the covenanting parties.
Positive Covenants – Imposed by earlier owner and states what subsequent owners must do e.g maintaining boundaries, maintaining the front garden.
Restrictive Covenants – States what owner must not do. May have significant impact on saleability of land or could be immaterial (e.g no livestock on plot in a residential area).

Offer of Advance

- Not a legal contract in itself, not binding on parties involved.
- It is an invitation to enter into a legal contract, subject to certain conditions being met

It can be withdrawn by the lender if:

- 1) Application consists false or inaccurate information.
- 2) The individual's financial or personal circumstances change.
- 3) Property offered for security for loan has suffered damage
- 4) Investigation of title carried out by the surveyor is unsatisfactory.

Report on Title

- A satisfactory report on title must be obtained before a lender enters into a binding contract with a borrower.
- The solicitor, who advises the lender, carries out this search.
- If search is unsatisfactory, solicitor must advise how this affects the security of property in question and how this can be overcome.
- Defective title indemnity insurance could be arranged to protect the lender and avoid further delays.

- It is now common for lenders to arrange title insurance policies on mortgages, which protect the lender and the owner against losses if full legal work is not completed.
- This reduces the legal work that has to be undertaken so that the mortgage can be completed quickly.
- Borrower will benefit from reduced costs as a result but must realise the consequences of defective title problems.

Title Problems

- If there are title problems a lender may insist on *revaluing the property* or may take out indemnity *insurance* to protect himself and /or the owner from others.

Legal charge (Mortgage deed)

- Executed on completion.
- Formal contract that binds both parties sets out the rights of the lender and the covenants of the borrower. Cannot be altered without the consent of both parties.
- Building insurance must be arranged as soon as contracts are exchanged, as the buyer becomes responsible for the property.

Table 1

<i>Lenders Rights</i>	<i>Borrowers Covenant</i>
Charge Capital, Interest and other fees	Make payments as required
Insure Property if borrower fails to do so and charge it to the mortgage account.	Insure property as required by lender
To let the property if it is repossessed.	Not to let the property without permission of the lender
Meet title, local authority or statue conditions if borrower does not.	Meet fully all regulations including appropriate legislation and local authority conditions.
Call in the whole debt if borrower defaults or is bankrupt or a compulsory purchase order is made on property	To allow the lender to inspect the property at any reasonable time.
Make Further Advances without creating a new Mortgage deed.	Comply with Title conditions such as positive and restrictive covenants and easements.
Transfer Mortgage to another lender if The borrower permits.	Comply with terms of lease if property is leasehold property.

Stage Payments

- Involves splitting up the loan for self build projects.
- Loan is released in three to four parts depending on agreement.
- Cost effective, savings are estimated at about 25% in comparison to buying an existing house.
- Lender prefers that builder is member of NHBC scheme; Zurich scheme or a qualifying supervising Architect supervises building.

Quality of Construction

- NHBC Scheme – -Introduced in 1965 and relaunched in 1988 as *build mark*.
- As part of build mark scheme builders must satisfy NHBC building standards.
- Financial constraints include £1,000,000 for new properties, £500,000 for converted properties.
- Only claims over £1,000 are dealt with, and total cover is for ten years.
- For the first two years, the build mark scheme will protect against defects or damages where the builder has failed to meet NHBC standards in full.
- For the next eight years, scheme provides insurance on damage over £1,000, in the building structure
- Claim must first be made to the builder, and will only go to NHBC if there is a disagreement.
- Zurich Mutual Insurance Scheme -Similar to above but covers a 15year period as opposed to a 10year period as with the NHBC.

The Consumer Credit Act 1974

- *Regulated by Office of Fair Trading*
- Regulates certain types of lending including personal loans and revolving credit.
- Loans, which are termed 'Regulated Mortgage Contracts' by the FSA, are not covered.
- Loans raised on the security of a dwelling but used for other purposes are uncovered.
- Only loans to personal borrowers
- Loans for mixed purposes are separated into regulated and unregulated parts
- Covers loans £25,000 and under except it is for an exempt purpose such as *purchase, alteration, improvement, or repair of a main dwelling or the original loan is with the same lender.*

- The annual percentage rate (APR –interest rate plus additional costs and fees charged while arranging the loan) must be quoted on all loans, to allow for fair comparison between lenders.
- In April 2008 the amount covered will be unlimited as the £25,000 limit on most loans are removed from 1/1/08.
- Office of fair-trading will impose financial penalties and discipline fraudulent firms.

The Consumer Credit Act 2006

- Updated version of the 1974 act.
- Provides better service levels for clients.

6/4/07

- In April 2008 the amount covered is unlimited as the £25,000 limit on most loans are removed, from 1/10/08.
- Loans for business purposes are exempt that exceed £25,000.
- Sole traders, partnerships or unincorporated associations with 3 or fewer persons are covered.
- High net worth individuals whose income and assets are above the threshold, can for go protection of the act, if an agreement is signed.
- Complaints are now referred to the Financial Ombudsman.

Data Protection Act 1998

- The FSA is a registered data controller.
- The Act explains concisely how data must be stored, used or accessed.
- Data includes electronic and manual records.
- Information must relate to a living individual.
- Data must be processed fairly and lawfully.
- Data must be obtained for specific and lawful processes.
- Data must not be excessive, must be relevant to purpose it is needed.
- Data must be updated and accurate.
- Data must not be kept longer than it is needed.
- Data must not be transferred to a country outside the EEA unless the country treats data like the EEA.
- Data must be processed in accordance to rights of Data Subject.
- Data must be corrected if it is wrong.
- Subject must be able to pay a fee of £10 for information and receive it within 40 days.

Data Subject- Person whose data is processed

Data Processor-Person who processes the data

Data Controller-‘Legal Person’ in charge of data processor could be a firm,

sole trader etc ensures that requirements of Act are met.

Information Commissioner – Man in Charge of all data controllers, who must be registered with him. Oversees the application of Data Protection Act.

Wills

- Must be in writing
- Must be signed in the presence of two witnesses, but not be signed in presence of beneficiaries or their spouses.
- Executor can be a beneficiary
- If person dies intestate (without a will), Personal Representative applies for *Letters of Administration*.
- If person dies testate (with a will), Executor applies for a *Grant of probate*. If person gets married after writing a will, the will is invalid unless written in contemplation of marriage in mind.

Codicil – Modifications within he will

Deed of Variation – Beneficiaries vary a will because of *Tax reasons*. All must be over 18 and must be in agreement. Must be executed 2 years of death. Inland Revenue must be informed within 6 months of execution.

House Buying Process (methods of purchase)

Private Treaty – Deal agreed between purchaser and seller

Auction – Deal agreed through bidding.

Buying at an Auction

- At the Auction the highest bidder buys the property.

Reserve price – Minimum price vendor is willing to accept. (interested parties can negotiate after the auction, if the house is not sold)

Main Issue – Once winning bid is accepted 10% deposit is paid and contracts exchanged on the day of the auction. Finance must be in place and mortgage arranged. The buyer needs to complete a survey, mortgage application and preliminary legal work before the auction.

Defects or issues identified do not release buyer from auction unless there are deception or title problems.

Property will need work in most cases so the buyer might need extra funds.

The Mortgage lender might place an undertaking or in fact a retention on the funds as recommended by the surveyor, if property requires repair; particularly in the case of older properties.