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Maskells Research – West Bromwich Court Case

Research:

West Bromwich lost Court of Appeal Case re Increasing interest payments on Mortgages without corresponding increase in base rates.

Language in Mortgage documentation "unclear"

Low Interest rates and higher costs blamed for increase in rate

Regulatory environment has increased Lenders' costs which they are seeking to pass on to Borrowers.

Basell III will make borrowing more expensive for Buy to Let Landlords.

Maskells Research Paper on The Leveraged Buy To Let Market due shortly.

In 2013 the West Bromwich Mortgage Company Ltd, a wholly owned subsidiary of West Bromwich Building Society decided to increase the interest rate margin on their tracker mortgages issued to certain multi-property Buy to Let Landlords who had mortgage loans with them. This decision affected Landlords who had taken out mortgages up to 2008

The question at hand was whether the language used in the Mortgage Agreement allowed the mortgage company to increase the margin without an increase in BOE base rate. The case made by the Property 118 Action Group was that the documentation had to be "clear, fair and not misleading" as defined in the FCA's Financial Promotions Regulations.

The Mortgage Company it was alleged, wanted to increase the interest rate margin because *"After careful consideration and in response to the unprecedented reduction in interest rates over recent years and <u>the increased relative cost in providing these loans</u>, the Society could not, in order to protect the best interests of members, ignore this clause…" (statement from West Bromwich dated 8th June 2016).* This clause, the company maintained, allowed them to vary the terms and conditions of the mortgage loans under certain circumstances so that the mortgage interest rate was more "*in line with the current market norm*"

It was also alleged that the company sought to impose a provision which would allow them to redeem the mortgage with 30 days notice. The Court of Appeal ruled that the company was NOT entitled to vary the mortgage rate on the loans absent a change in the Bank of England base rate NOR was it allowed to call the mortgages absent the default of a borrower.

IT seems to us that the devil is yet again in the detail: had the terms of the original mortgage contained clear provisions which would allow the mortgage company to vary interest rates without an increase in the Bank of England base rate or that the company could call the mortgages with 30 days notice, this case may never have been brought.

Notwithstanding this, there is one part that interests us, and it is underlined in the statement from the Society above. This increase in relative costs takes into account the additional capital the society has had to set aside against it's Common Equity Tier 1 Capital Ratio (CET1) as well as other provisions. In it's Pillar 3 Capital Disclosures for year ended 31St March 2014 the Society showed a CET1 prior to regulatory adjustments of £417.6m and post adjustment to £363.2m. There are many factors which led to this but one foot note is of interest "*a 50% weighting is applied to mortgage pipeline ad committed facilities as per the Basell III leverage ratio framework*".

What does this mean? The cost of holding mortgages on balance sheet has increased with no balancing increase in the interest margin of, in this case, the mortgages issued the multi-property buy to let landlords who brought this action. We can be quite certain that language in the mortgage documentation from all lenders will change, if it has not already, to take into account the additional costs that Banks and Building Societies will face under Basell III. Buy to Let mortgage rates will increase and Maskells will shortly be issuing a research paper on this and the possible effects on the market.