

## Managing buy to let arrears

Recent weeks have seen extensive media coverage of the challenges both lenders and borrowers are currently facing in the buy to let sector. CML buy to let mortgage figures for Q1 2008 show mortgages in 3 months plus arrears were 21% higher than for the same period in 2007. All indications point to arrears in this sector increasing at a gathering pace. This commentary highlights the challenges lenders face in managing buy to let arrears portfolios and emerging trends we are seeing in the sector.

The major challenges for lenders are minimising losses on sale in a market sector now at risk of high shortfalls and handling the unique issues presented when attempting to take possession of buy to let properties.

### Options once arrears have accrued

If a tenancy is unauthorised which is invariably due to either a mortgage condition which deems it to be so as soon as arrears accrue or because specific requirements relating to the form or term of the tenancy have been breached, a lender is able to commence possession proceedings in the normal way and should be able to defeat any claim by the tenant which would prevent vacant possession being secured.

The appointment of an LPA Receiver is an option for those lenders who have provision for this in their mortgage conditions. Certain lenders appoint as a matter of course whilst others are more selective using Receivers in cases where the tenant has acquired rights to occupy as a result of:

- The tenant being in occupation of the property prior to and at the time the buy to let mortgage was entered into by the borrower so claiming an overriding interest.
- The borrower having complied fully with provisions in the Mortgage Deed, Mortgage Conditions and Special Conditions in relation to the letting of the property.

The decision as to whether to appoint an LPA Receiver is one that will be made based on the circumstances of each case or as a policy across a portfolio.

### Unique challenges of buy to let arrears

The types of issues which commonly arise for buy to let lenders in arrears cases are claims by tenants that they have rights which pre-exist the lenders (overriding interests), a growing trend of tenants claiming that they have paid a lump sum of rent at the beginning of the tenancy, cases involving borrowers exceeding lending criteria on maximum property numbers and undisclosed builder incentives on new build flat buy to lets.

The lack of disclosure of builder's incentives has led to the CML introducing new standards for industry professionals acting for lenders on new build property transactions. The standards reflect lenders concerns that the current valuation and conveyancing processes do not always capture discounts and other incentives negotiated with developers when purchasing new build property. The impact of this is that the advance is based upon a price higher than that actually paid by the borrower and this has led to substantial losses following possession and sale. The plan is to introduce in September 2008 a new 'disclosure of incentives' form which builders or developers of any newly built, converted or renovated property will be required by lenders to complete. This requirement will be backed up by new provisions in the CML Lenders' Handbook.

On the Court front, a recent trend seen in Portsmouth County Court is that requiring lenders to submit documentation to justify why a tenancy was unauthorised. The view taken by the Court was that unless there is express evidence to the contrary, the tenant is deemed to be authorised by virtue of the fact that the mortgage has been taken out specifically for buy to let purposes. This decision is open to challenge as each case must be considered on its individual facts having regard to the mortgage conditions and the tenancy terms but it illustrates the scrutiny buy to let cases are under.

### Summary

There can be no doubt that the buy to let market is a challenging environment particularly for the amateur landlord relying on rental income in order to meet mortgage payments. This type of landlord often has several buy to let properties and may be receiving income from some of the properties but not be able to cover empty periods in others. The credit crunch has stretched landlords further especially those on fixed rate mortgages that are expiring where attractive alternative products are not available.

Whilst the rental market generally is strengthening, and this is predicted to continue whilst conditions stabilise as individuals look to this route rather than purchase, there are challenges to face for landlords and lenders brought on by the credit crunch, increasing costs of living and equity shrink.