Britain: “Liar loans” drive hundreds of thousands into debt

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A recent report from the UK Citizens Advice Bureau (CAB) has revealed that hundreds of thousands of people are being driven into debt, end up in court and face the loss of their homes because of irresponsible lending practices, bad advice and downright fraud. For people who have longed to buy their own home their dream has turned into a nightmare.

The report *Set Up To Fail: CAB Clients experience of Mortgage and Secured Loan Arrears Problems (December 2007)* says mortgage brokers are providing loans—called appropriately “liar loans” or self certification loans—to people with poor credit records and “little or no financial acumen” without them having to provide proof of their incomes. Most people interviewed in the report said they relied on the broker for advice and guidance but many had not even been told the serious consequences of falling behind with repayments.

The report is also highly critical of the regulatory authorities and the Labour government, saying there are not enough safety nets to protect vulnerable borrowers.

CAB Chief Executive David Harker said, “The cavalier behaviour of some brokers and sub-prime lenders is seriously undermining home ownership and hitting the most vulnerable borrowers hardest. Our research suggests that many aspiring homeowners have been mis-sold unsuitable and costly home loans that are doomed to fail from the start. Many sub-prime lenders are flouting the rules on responsible lending by granting loans when it’s clear the borrower will not be able to afford to repay it from the very outset, then getting tough immediately things go wrong. Far from providing housing security and a valuable asset, home ownership has proved a fast track to debt and homelessness for many vulnerable borrowers on low incomes.”

According to the CAB report, which was based on 1,200 case studies from 360 advice centres across the UK, the organisation was involved in over 57,000 cases of mortgage and secured loan arrears last year (2006-07), an 11 percent increase on the previous year. Research suggested as many as 770,000 people had missed at least one mortgage or secured loan payment in the previous 12 months.

The report shows how the majority of people coming into CAB offices seeking mortgage advice have been rejected by the High Street banks and mortgage lenders and are forced to take loans from sub-prime lenders at much higher rates of interest. It reveals that “more than a third had household incomes below the UK poverty line, one in five was reliant on means tested benefits, and nearly 70 percent had outstanding unsecured debts averaging £22,000.”

More and more of people’s income is taken up with mortgage repayments of one kind or another. For a third of all clients interviewed in the CAB report, their combined mortgage and secured loans payments were over half their income; for 12 percent of interviewees their repayments were an unbelievable 70 percent of their income.

One case study in the report involved a 47-year-old local authority tenant living in Yorkshire who exercised the right to buy the property where he was living. A broker persuaded him to say that he was self-employed on the mortgage application form even though he was in receipt of incapacity benefit and disability allowance because of the severe mental health problems he suffered. Some months after completion of the sale the mortgage interest rate increased. Because he was unable to keep up repayments the lender took court action for possession of his house, leaving him facing homelessness and still in debt.

There has been a massive increase in the number of house repossessions recently, with some economists saying levels are now close to those seen when house prices slumped in the 1990s. The Council of Mortgage

Lenders reports that repossessions rose by 75 percent last year to reach 30,000 and suggests this figure could reach 45,000 in 2008.

The CAB has also investigated the number of repossession cases listed in 23 county courts in January 2007 and found that sub-prime lenders were responsible for a huge number of them—“in some cases the equivalent of ten times more than mainstream lenders.” It points out that although many borrowers do not turn up to court thinking that they will automatically lose, the behaviour of the lender is so bad that many judges are forced to side with the customers.

The increasing difficulties facing homeowners is reflected in the extraordinary growth of the debt collection industry. It has quadrupled in size since 2003, from handling £8.6 billion worth of debt to £22.7 billion now. One of the most disturbing aspects highlighted by the report is the mushrooming of companies that are like vultures waiting for their next meal, preying on people who no longer have any solution to their debt problems other than selling their house and renting it back.

The evidence suggests that “homeowners in a financially and emotionally vulnerable situation end up selling their houses for much less than they are worth, in return for a tenancy that offers little security of tenure.” The state-run income support mortgage interest scheme and private mortgage payment protection insurance (MPPI) policies (held by one quarter of homeowners) are supposed to help in such situations. However, the former is woefully inadequate to protect those in greatest need of help and insurance companies often find ways to avoid paying out the latter.

A CAB office in south London, for example, reported how a woman with mortgage arrears had been signed off work by her doctor because of the stress involved in trying to keep up with the terms of a court order suspending possession of her house. After her claim on a MPPI policy was turned down she resorted to a sale and rent-back company and signed an agreement without receiving any advice or comparative quotes from the salesmen who visited her. While the property was worth £350,000, she got only £200,000—just enough to pay off her mortgage and unsecured debts. Although she also received a six-month £750-per-month tenancy agreement, the landlord then wanted to put it up to £1,300 per month, saying it had been incorrectly assessed. Shortly afterwards the poor woman was back in court facing possession for rent arrears.

The report also quotes evidence from the housing charity Shelter (http://england.shelter.org.uk/home/index.cfm) about the increasing use of credit cards to pay mortgages or rent, which has affected nearly 1 million people in the 12 months up to October 2007.

Shelter’s chief executive Adam Sampson said, “Clearly, this is a huge problem which will only become more widespread as housing costs continue to rise. We would urge anyone struggling with the cost of their mortgage or rent to seek independent financial advice. The number of people hit by the credit crunch, interest rate hikes and unaffordable housing costs are rapidly rising.”

“For many people trying to keep a roof over their head, desperation is driving them to short-term, high-cost borrowing. Ordinary people are being forced to seek more risky and expensive ways to stave off the threat of eviction and repossession,” he added.

The loans have been used to transfer wealth into the hands of the ruling elite, and at the same time become a means of speculation. Backed by the big banks and brokerage houses, mortgage companies aggressively marketed home loans to households that in the past would have never been approved for such loans. Home buyers were assured that they were protected by rising home prices, which would enable them, if they found themselves in economic straits, to sell their properties and have more than enough money to pay off their outstanding balances. With house prices falling throughout the country this will no longer be the case and portends a social disaster for many people in 2008. Auditors KPMG have predicted that personal insolvencies in England and Wales will rise to more than 130,000 from 109,615 in 2007.