



North East Property Buyers: sale and rent back schemes leave a nasty taste in the mouth for all concerned

The Supreme Court has handed down its long-awaited judgment in *Scott v (1) Southern Pacific Mortgages Limited (2) Mortgage Express [2014] UKSC 52*. We examine the case and why the Law Lords reluctantly reached the conclusion that tenants in sale and rent back schemes could not defeat the interests of the landlords' lenders.

The background

The *Scott* case is a test case stemming from a scheme run by the so-called "North East Property Buyers" (NEPB), a group of individuals who bought homes from borrowers experiencing problems meeting their mortgage repayments (at a severe discount to the true market value). In return, the customer was led to believe that he or she could continue to live at the premises on an indefinite basis under a lease (for a nominal rent), and (in this case) that the tenancy would be inherited by her son on her death.

In most cases (including the current one, where the purchaser was a Ms Wilkinson) the customer did not know that the purchase of their property was financed by borrowing raised by the purchaser, and secured by a mortgage on the freehold of the property they had just sold.

When the relevant buyer under the North East scheme defaulted on their payments to the bank, the bank sought to sell the underlying property with vacant possession - i.e. free of the customer's lease. Understandably the affected customers protested that this was manifestly unfair and the current action was brought as a test case to determine what the parties' respective rights were.

The issues

The issues for the court were: (i) whether the sale and rent back arrangements conferred an "overriding interest" (a proprietary as opposed to a merely personal right) which permitted Mrs Scott to remain in occupation; and (ii) if the answer to (i) was yes, whether case law prevented Mrs Scott from asserting her rights in competition with the lender.

What did the court decide?

The Supreme Court carefully examined the case law and the provisions of Section 116 and 132 of the Land Registration Act 2002. Although the sale and rent back arrangement bore the hallmarks of "proprietary estoppel", no such estoppel could become an interest in land before the purchaser himself became the owner

of the property. The issue was whether the transfer of the land to the purchaser and the mortgage granted by him were one indivisible transaction, or whether a moment in time existed between them, during which Mrs Scott could acquire her proprietary interest. With regret, the court decided that the mortgage and transfer were indivisible, and in any event Mrs Scott's rights would only become proprietary if "fed" by Ms Wilkinson's acquisition of the property.

The need to consider the second issue did not arise as a result. Nevertheless, the court gave its view that even if Mrs Scott had acquired a proprietary interest, the indivisible nature of the transfer of the land and the mortgage granted by Wilkinson meant that the lender would still have enjoyed priority.

What does this mean in practice?

This is an unfortunate and somewhat disheartening case. The court was faced with the unpalatable task of balancing the interests of a duped individual on the one hand, and an institution which had financed the acquisition of the relevant property (and was unaware of the underlying transaction – indeed the tenancy granted to Mrs Scott was in breach of the terms of the mortgage) on the other. Established case law, coupled with the negative impact of allowing the supremacy of onerous, low value leases with a depressing effect on the value of the mortgaged property over the rights of a bank seeking sale, all legislated against the hapless seller, Mrs Scott.

Unfortunately this decision affects a substantial number of individuals who have been taken in by the NEPB scheme. The courts' hands were tied by well-established law. It remains to be seen if legislation will be passed to provide some remedy to victims of such arrangements.

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