

WRAP-UP MORTGAGES: A CREATIVE ALTERNATIVE TO FORCED AUCTIONS IN KENYA

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A recent Business Daily article on *"Tycoons scramble for posh homes in auctioneers' yards"* dated 24th July, 2025 has once again drawn attention to the sharp rise in public auctions of high-end properties across Kenya.

These auctions, while a legal remedy for lenders, often lead to significant financial losses for homeowners since auction prices tend to be far below market value, reputational harm and distress for property owners, and longer recovery timelines for lenders as they struggle to dispose of prime assets. Distressed auctions also come with the uncertainty and risks of litigation and contested ownership.

As an alternative, wrap-up (wrap-around) mortgages are proving to be an innovative, win–win solution for all parties involved.

WHY WRAP-UP MORTGAGES MATTER

Rather than resorting to foreclosure and forced auction, a lender can allow a property owner to transfer the property to a new buyer under a wrap-up structure. This ensures that the original mortgage remains serviced, protecting the bank's exposure, the homeowner preserves equity and avoids the stigma of a public auction, and the buyer accesses prime real estate through flexible financing, bypassing traditional lending hurdles.

On the other hand, buyers benefit as they can purchase properties in a controlled and secure environment without the uncertainties of participating in an open auction. For lenders and homeowners, this model helps to avoid costly, protracted litigation that often accompanies distressed property auctions.

This approach is increasingly relevant in Kenya's high-end property market, where liquidity pressures have been forcing distress sales.

WHAT IS A WRAP-UP MORTGAGE?

A wrap-up mortgage is a secondary financing arrangement in which a seller with an existing mortgage finances a buyer's purchase by "wrapping" a new loan around the seller's outstanding mortgage.

How it works: the buyer and seller agree on a price; the buyer pays a deposit and makes monthly instalments to the seller (or into an escrow account); the seller uses these instalments to continue servicing the existing mortgage; and any difference between the buyer's payments and the seller's mortgage obligations becomes the seller's profit.

BENEFITS OF WRAP-UP MORTGAGES

- Enables buyers who may not qualify for bank loans to access property.
- Allows faster property transactions, bypassing lengthy bank approval processes.
- Provides an income stream for sellers through the interest margin.
- Offers a softer exit option for lenders compared to distress auctions.
- Reduces risks and uncertainty associated with auctions, while avoiding costly litigation.

KEY LEGAL AND REGULATORY CONSIDERATIONS

For a wrap-up mortgage to work effectively in Kenya, it is crucial that the lender provides consent, as most mortgage instruments include "no transfer without consent" clauses. The transaction must be supported by comprehensive documentation, including a detailed sale agreement, a wrap-up financing agreement, and security instruments such as a second charge or lien.

Compliance with the Land Act, 2012, the Sectional Properties Act, 2020, the Stamp Duty Act, and the Banking Act with CBK Prudential Guidelines is mandatory. Tax implications must also be taken into account, as any interest earned by the seller is taxable, and capital gains tax may apply.

Finally, clear and transparent terms must be agreed upon to manage risk effectively and safeguard the interests of both the buyer and the seller.

PROTECTING THE BUYER'S POSITION

Buyer interests can be strengthened through direct payments to the lender via an escrow arrangement, a variation of the initial mortgage so that instalments are applied directly towards clearing the bank's charge, and negotiated release of deposit funds to the seller (with the lender's written consent) to allow the seller to buy a smaller replacement home, such as a townhouse or an apartment, without affecting the lender's security.

ILLUSTRATIVE EXAMPLE: PRIME LAVINGTON VILLA

- Property: KES 75 million villa in Lavington
- Outstanding mortgage: KES 30 million at 13% interest
- Solution:
    - Buyer James pays a deposit of KES 30 million
    - With the bank's consent, the seller Grace uses this deposit to purchase a smaller townhouse or an apartment
    - The balance of KES 45 million is financed by Grace at 15%
    - James pays KES 675,000 monthly into an escrow account:
        - KES 325,000 services the original mortgage
        - The remainder is Grace's profit

Outcome: James acquires the villa without taking a new bank loan, Grace avoids a forced auction, services her mortgage, and secures a new home, and the lender continues to receive payments, maintaining its security.

WHEN WRAP-UP MORTGAGES ARE USEFUL IN KENYA

Wrap-up mortgages can be useful in a variety of scenarios. They are particularly effective for developers or individual sellers looking to sell quickly in a slow market. They also help buyers without sufficient credit history, such as diaspora Kenyans returning home, who may not have easy access to traditional bank financing.

In high-interest environments, wrap-up mortgages present an attractive alternative to conventional bank loans. Most importantly, they serve as a foreclosure avoidance mechanism, enabling lenders and property owners to restructure property disposals instead of resorting to auction. These arrangements also allow buyers to acquire prime assets without the uncertainty of bidding at auctions and help lenders and homeowners avoid disputes and litigation often associated with distressed sales.

They also support lenders by enabling a controlled and transparent asset transfer, ensuring continuity of repayment, and avoiding reputational risks of auctions. For buyers, these arrangements open access to opportunities that might otherwise be missed, while for sellers, they create an orderly path to liquidity and stability.

HOW CM ADVOCATES LLP'S REAL ESTATE BANKING & FINANCE DEPARTMENT CAN ASSIST

CM Advocates LLP has one of Kenya's most specialized Real Estate, Banking and Finance departments. In the context of wrap-up mortgages, our services include:-

- Strategic advice: Helping lenders, property owners and buyers avoid foreclosure by

structuring wrap-up mortgage solutions instead of distressed auctions.

- End-to-end structuring of wrap-around financing arrangements tailored to both high-end and middle-income markets.
- Lender engagement: Negotiating with banks for consent, partial releases of deposits, and variation of existing mortgage terms to allow these transactions.
- Comprehensive legal documentation: Drafting, reviewing and perfecting Sale Agreements, Wrap-Up Mortgage Agreements, Escrow Instructions, Second Charges, and Deed variations.
- Regulatory compliance: Ensuring adherence to Kenyan land, tax, and financial services laws.
- Dispute avoidance and resolution: Creating safeguards to minimize disputes and representing clients in case of default or breach.
- Tax advisory: Advising on VAT, income tax, and capital gains tax implications of such structures.

Our experience in high-value residential, commercial, and development finance transactions allows us to effectively represent and advise lenders, homeowners, and buyers, ensuring the successful implementation of innovative financing models like wrap-up mortgages.

KEY TAKEAWAY

Wrap-up mortgages provide a strategic, humane, and commercially sound alternative to forced auctions, benefitting property owners and borrowers facing foreclosure, buyers seeking opportunities in distressed assets, and lenders looking for effective solutions. They allow buyers to purchase properties in a safe and predictable way without the uncertainties of auction processes and help lenders and homeowners avoid the expense and complexity of litigation that often arises with distressed properties.

Property owners, borrowers, buyers, and sellers facing distressed property challenges and needing innovative solutions or secure transactions are strongly encouraged to contact CM Advocates LLP for expert advisory and structured support.

For comprehensive advisory on secured lending transactions, acquisition of property from lenders, structuring wrap-up mortgage solutions, dispute management, or cross-jurisdictional guidance, please contact:

For more information or legal structuring support, contact us at:-

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