DRN-3039675

The complaint

Mrs W complains that Bank of Scotland plc wouldn't offer her a lower interest rate product, or capitalise the arrears on her mortgage account.

What happened

Mrs W has a repayment mortgage with BoS. In 2007, she took out a fixed rate of 6.09% which ran until 31 January 2018. Unfortunately, during that 10-year period, Mrs W struggled with financial difficulty due to a change in her circumstances, and an arrears balance accrued on the account.

After the fixed rate ended in January 2018, Mrs W had several conversations with BoS about her situation. She advised that she was a full-time carer, and so was making the monthly payments through benefit payments and support from family. She was taking some part time work where she could. She was prioritising the mortgage and made it clear she wanted to do all she could to avoid any repossession action or the need to sell her property. Short term arrangements were set throughout 2018, and whilst there were some periods where the benefit payments were delayed, the contractual monthly payments (CMP) were being made in most months, as well as contributions to the arrears.

Other options for the mortgage were explored such as a term extension, but BoS said that as the term already ran past Mrs W's expected retirement age then they wouldn't extend it further. Mrs W was expecting to be able to clear the arrears within a couple of years using a pension drawdown, so short term arrangements continued to be agreed.

Throughout 2019 and 2020 more short term arrangements were agreed, and several conversations were had about Mrs W's circumstances and the mortgage due to the arrears that remained on the account. Mrs W asked about lower interest rates and capitalisation of the arrears on the mortgage, but neither of these were agreed. Unfortunately, the impact of covid-19 affected Mrs W's ability to consistently meet the CMP during 2020. Although a payment deferral was never agreed.

Mrs W complained about the way BoS were treating her, and specifically that they hadn't offered her a lower interest rate, and the bank issued their final response in May 2020. They explained that as Mrs W's account had been in arrears since her fixed rate product ended, then she was not eligible for a new interest rate product. They said the account was on hold due to the impact of covid-19 and so no further action was being considered at that time. They didn't uphold the complaint.

Mrs W also complained about the fact the bank refused to capitalise her arrears when she'd been told they would consider doing so. BoS issued a separate final response letter about that and offered Mrs W £200 to apologise for the fact she'd been given incorrect information. Mrs W had been told BoS would consider capitalisation if she made three consecutive monthly payments. BoS confirmed in their final response letter that this was wrong, and she needed to make 12 monthly payments before that would be considered.

Mrs W brought her complaint to our service and our investigator looked into things. She didn’t think BoS had acted unfairly by not offering Mrs W an interest rate product. She agreed that Mrs W had been given incorrect information about capitalising the arrears, but she felt BoS had done enough to put that right.

Mrs W didn’t agree. She said she couldn’t understand why the bank wouldn’t give her a lower interest rate product when what she was paying on the standard variable rate (SVR) was more than what the new monthly payment would have been. She’d demonstrated she could afford the higher monthly payments so didn’t think it was fair that she was refused a product.

Our investigator wasn’t persuaded to change her mind, so the complaint’s been passed to me to issue a decision.

My provisional decision

I issued a provisional decision on 10 January 2022, and this is what I said.

“I’ve considered all the available evidence and arguments to decide what’s fair and reasonable in the circumstances of this complaint.

It’s clear to see that Mrs W has been through a difficult time over the years, and I’m sorry to hear about what she’s been through. Having reviewed the contact notes and the history of this mortgage account, I think it’s clear that Mrs W has consistently engaged with BoS about her circumstances, and has been prioritising her mortgage payments in order to keep to the arrangements set. Considering all the evidence, whilst I’m satisfied that BoS showed some forbearance in agreeing short term arrangements with Mrs W, and re-setting her payment dates due to changes in benefits payments, I’m not satisfied they’ve done as much as they could, and in my opinion should, have done to help Mrs W to manage this mortgage in the long term.

Throughout 2018 and 2019, BoS were setting arrangements with Mrs W that required her to pay her CMP of around £1,400 plus a contribution of around £200 towards the arrears. Mrs W’s income largely came from benefits she was receiving as a result of her caring responsibilities, although she was taking on part time work where she could. I understand the Department for Work and Pensions (DWP) were also contributing to the interest payments on the mortgage. During that two year period, it seems that Mrs W was able to make those agreed payments. I appreciate there were times when payments were made late, or they were a little bit short. But from the notes it seems this was largely due to delays or problems with the benefits payments being received on time, and were ultimately made to the account.

I’ve considered BoS’s policy in regards to capitalising arrears on a mortgage account, and also eligibility for interest rate products. Having thought carefully here about Mrs W’s overall circumstances and what the bank could have done to help the future sustainability of the mortgage, I think there was more BoS could have done to help make this mortgage more affordable for Mrs W.

By early 2019, Mrs W had a 12 month track record of being able to afford a significant payment that was higher than her CMP. I think at that point, Mrs W should have been given the option to capitalise her arrears onto the mortgage, which would have led to her becoming eligible for an interest rate product. That would have been in line with the bank’s own policy. It seems that the income and expenditure assessments Mrs W completed for the bank showed that she could afford to make the payments required under the arrangements. And BoS have provided our service with information about what capitalisation and an interest rate product would have meant for Mrs W’s monthly payments. This information shows that had *these measures been put in place, Mrs W's monthly payments would have reduced to less than what she had already been paying.*

I appreciate Mrs W hadn't specifically asked about capitalising her arrears until more recently, but she had asked about interest rate products on at least two occasions and was told she wasn't eligible for a product due to the arrears. The notes show that based on Mrs W's existing payment arrangements that the bank kept arranging, it would have taken Mrs W 11 years to clear the arrears on the mortgage. Whilst this is within the existing mortgage term, it would have meant that whilst the arrears were still present on Mrs W's account for that period, she would have remained trapped on the standard variable rate as she would never have met the bank's eligibility criteria for a product. However, if the arrears had been capitalised, as Mrs W had demonstrated she could afford, she could have taken out a lower interest rate which would have reduced her monthly payments, as well as resulted in the mortgage being up to date and fully redeemed within the term.

I think the bank had a responsibility to explore both long term and short term forbearance options to help Mrs W get the mortgage back on track and I think this option should have been considered and suggested.

However, I do also acknowledge that during the time that's passed since these conversations, Mrs W has unfortunately been impacted by the global pandemic, and so she wasn't able to make all of her CMPs on time during 2020. I can see from the notes that Mrs W did request a payment holiday because of this, but it doesn't seem that this was granted. It's unclear why, but based on what I've seen – and subject to any further information being provided - I think Mrs W would have been eligible for a payment holiday under the regulator's guidance at the time. Having said this, Mrs W was able to make some payments to the mortgage during that period, and it was in her interests to pay as much as she could to reduce the longer term impact any payment holiday may have had.

BoS have said that because of the payment history during 2020 and 2021, even if they had applied a lower interest rate product to the account, after capitalising the arrears in 2019, there would still be arrears on the account now. And I do understand that and have thought about it carefully. But looking at the calculations the bank have provided this service, if they had applied lower interest rates to Mrs W's accounts from 2019, the arrears position would have gone from £26,489.29 to £3,359.30 as of November 2021. That is a significant difference and I'm satisfied it would be in both parties' interests to make those changes to the account.

Having considered what Mrs W has said to both the bank and this service, I'm persuaded that the lower arrears balance (less than three monthly payments) would be manageable for her to clear in a short period of time. Those recent arrears have accrued as a result of a global pandemic that has impacted a significant number of borrowers and could not have been foreseen. And therefore, I consider Mrs W should be given the opportunity to clear those arrears in line with the regulator's guidance to lenders for offering forbearance to those borrowers impacted by the pandemic. From everything I've seen, I'm satisfied these measures should enable Mrs W to get this mortgage back on track and sustain it in the long term.

BoS have also said that applying an interest rate product to Mrs W's mortgage would result in an Early Repayment Charge (ERC) becoming payable if the mortgage was redeemed early. They're concerned that whilst arrears remain on the account, legal action may still be taken, and this would result in more charges for Mrs W than if the product wasn't in place. I think this is a relevant and important consideration.

At the time Mrs W was asking for help in 2018 and 2019, she was consistently paying more *than was required under the CMP. I don't think at that time, falling back into arrears was a concern for Mrs W as she was taking steps to reduce the arrears that were already in place. So I'm satisfied the risk of applying an interest rate product with an ERC attached was low at that time. The arrears that have subsequently accrued on the mortgage were a result of the pandemic. And as I've said above, both parties will need to engage about how these new arrears will be repaid. Mrs W should be given an appropriate amount of time to consider her options in how to repay those arrears before BoS consider starting any legal action to recover them.*

Overall, I'm satisfied based on the evidence I've seen, that capitalising Mrs W's arrears and offering her a lower interest rate in 2019 would have been appropriate forbearance to help Mrs W get this mortgage back on track. I'm satisfied her payment history, as well as the details given about her income and expenditure, demonstrated her ability to sustain the mortgage in that way in the long term. And so I think it's something BoS should have put in place for her. As a result, I intend to uphold this complaint.

As I intend to uphold Mrs W's complaint about how the bank handled things in 2019, I haven't considered whether BoS should have capitalised Mrs W's mortgage arrears in early 2020 as they wouldn't have existed.

Putting things right

In order to put things right, I intend to direct BoS to re-work Mrs W's mortgage account to put it back into the position it should have been in had they capitalised her mortgage arrears and given her a lower interest rate product. This means:

- *Capitalising Mrs W's mortgage arrears as they stood in February 2019;*
- *Applying the lowest available interest rate product that Mrs W would have been eligible for in February 2019. The bank have told this service that would have been a two-year fixed rate of 2.79%;*
- *Applying the lowest available interest rate product that Mrs W would have been eligible for on expiry of the above rate in May 2021. The bank have told this service that would have been 1.4% fixed for either a three year or five year period. Mrs W should get the opportunity to choose which she'd prefer;*
- *Refunding any fees or charges that were applied as a result of the arrears on the account that wouldn't have been there following the above reconstruction;*
- *Amending the way the bank has reported Mrs W's mortgage to credit reference agencies – to reflect the reconstructed mortgage position.*

Having considered all the circumstances I'm also persuaded that Mrs W has experienced distress and inconvenience as a result of BoS's actions, and the way they've handled Mrs W's mortgage since she's been asking for lower interest rates. Had BoS put in place the forbearance I've set out above, I think it would have saved Mrs W a lot of stress and worry about her ability to make her mortgage payments, and also the time and stress of having to call the bank and re-set arrangements every few months. The bank have discussed potential legal action with Mrs W on more than one occasion and I think this could have been avoided. Given Mrs W's particular circumstances, I think an award of £750 should be paid to Mrs W to compensate for this. That is on top of the £200 BoS have already paid in relation to the incorrect information given."

Responses to my provisional decision

Mrs W accepted my provisional decision.

BoS responded and said, in summary:

- During the period February 2018 to January 2019 inclusive, Mrs W only made payments of the CMP or more in five months. She underpaid in seven of those months. Whilst some months did have overpayments, they weren't sufficient to cover the underpayments.
- For customers with arrears of more than 12 months on the mortgage account, BoS's policy requires 12 months of consecutive payments of the CMP or more to be made in order to qualify for capitalisation. This is because they have an obligation to be confident about ongoing affordability.
- Capitalising arrears should only be done as a last resort, and BoS don't think they'd reached a last resort as Mrs W had mentioned lump sum payments she was expecting which would have helped to clear the arrears.
- Despite the fact that Mrs W has not met the requirement of maintaining payments for 12 consecutive months, BoS are willing to offer capitalisation now based on Mrs W's most recent payment history if she can demonstrate through an income and expenditure assessment that she can maintain the payments.

What I've decided – and why

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

Having done so, whilst I've thought carefully about the points BoS have made, my decision remains unchanged. I'll explain why.

I set out in my provisional decision that during the 12 month period leading up to February 2019, Mrs W wasn't always able to make the full CMP on time each month. But the notes on the account suggest this was largely due to problems with Mrs W's benefits being paid on time rather than an ongoing affordability issue. I also think it's relevant to note that for the first half of 2018, BoS were including payments towards the arrears in their calculation of Mrs W's CMP and this wasn't rectified until June, when the CMP reduced by around £200. So for the first half of 2018, Mrs W's CMP was higher than it should have been. And looking at the 12 months' payments as a whole, when you include the overpayments Mrs W made, she had only paid slightly under (less than half of one month's CMP) what she should have done even on that higher CMP, before she then made overpayments again in early 2019.

Whilst I appreciate BoS wanted to ensure that Mrs W could afford to maintain the monthly payments before agreeing to lock her into an interest rate product, they were measuring her ability to afford those payments whilst her mortgage was on the SVR. If Mrs W's mortgage arrears were capitalised, and she had taken out a new interest rate product, her monthly payments would have been lower than what she had been paying. And I think Mrs W had provided sufficient evidence to show she could afford those payments.

BoS have said that capitalisation should only have been considered as a last resort, and they didn't think they'd reached that point, as Mrs W had mentioned she was expecting lump sum payments in the future. When arrears are capitalised onto a mortgage account, more interest becomes payable on those arrears over the term of the mortgage than if they were cleared separately through an arrangement, or repaid in a lump sum. So generally, where there are viable options available to clear the arrears more quickly, that can be preferable to adding them to the mortgage balance.

Mrs W did mention at points during 2018 that she was expecting some lump sum payments to be made to her. She made reference to a drawdown pension and an insurance premium refund she was expecting. I think it would have been reasonable for BoS to take that information into account when discussing Mrs W's options with her in relation to the future payments to the mortgage account.

But during those conversations it was clear that Mrs W's main concern was clearing the arrears balance so that she could take out a new interest rate product and reduce her monthly payments. I think if BoS had explained the options Mrs W had available to her at the time, i.e. capitalising the arrears and taking out a lower interest product, or staying on the SVR until she received the expected lump sum payments and could clear the arrears in one go, then Mrs W would have preferred to have capitalised the arrears and reduce her payments as soon as she could. I don't think it would have been irresponsible or unfair of BoS to agree to that given the benefits that would have resulted and Mrs W's priorities at the time. During the conversations Mrs W had with BoS during that time, she was consistently asking what else could be done to bring her monthly payments down, and so I'm persuaded that BoS should have discussed the option of capitalising Mrs W's arrears with her, and had they done that, she would have agreed to it.

Putting things right

In order to put things right, BoS should put Mrs W's mortgage back into the position it should have been in had they capitalised her mortgage arrears and given her a lower interest rate product in February 2019. This means:

- Capitalising Mrs W's mortgage arrears as they stood in February 2019;
- Applying the lowest available interest rate product that Mrs W would have been eligible for in February 2019. The bank have told this service that would have been 2.79%;
- Applying the lowest available interest rate product that Mrs W would have been eligible for on expiry of the above rate in May 2021. The bank have told this service that would have been 1.4%;
- Refunding any fees or charges that were applied as a result of the arrears on the account that wouldn't have been there following the above reconstruction;
- Amending the way the bank has reported Mrs W's mortgage to credit reference agencies – to reflect the reconstructed mortgage position.

Having considered all the circumstances I'm also persuaded that Mrs W has experienced distress and inconvenience as a result of BoS's actions, and the way they've handled Mrs W's mortgage since she's been asking for lower interest rates.

Had BoS put in place the forbearance I've set out above, I think Mrs W would have been saved a lot of stress and worry about her ability to make her mortgage payments, and also the time and stress of having to call the bank and re-set arrangements every few months. BoS have discussed potential legal action with Mrs W on more than one occasion and I think this could have been avoided. Given Mrs W's particular circumstances, I think an appropriate award of £750 should be paid to Mrs W to compensate for this. That is on top of the £200 BoS have already paid in relation to the incorrect information given.

My final decision

Considering everything, for the reasons I've explained, I uphold this complaint and direct Bank of Scotland plc to put things right in the way I've set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs W to accept or reject my decision before 10 March 2022.

Kathryn Billings
Ombudsman