

The complaint

Mr A and X complain that Yorkshire Building Society (YBS) mis-sold their mortgage. They said they wanted to make overpayments to reduce the term of the mortgage. But they later discovered that the overpayments had not reduced the term of the mortgage as they'd been led to believe.

What happened

In 2021, Mr A and X found out that YBS had not been using the overpayments to reduce the term of the mortgage. YBS said the overpayments reduced the balance, but the monthly payments were reduced each year in an annual review.

Mr A and X complain that YBS did not use the overpayments to reduce the term of the mortgage when they'd made it clear that was a priority for them.

Subject to any further submissions, my provisional decision was to uphold the complaint. My provisional findings, which form part of this decision, were:

The ability to make overpayments to reduce the term of the mortgage was clearly one of Mr A and X's stated needs when they took out the mortgage. YBS recommended a mortgage that had a facility that allowed overpayments and to reduce the mortgage term by what it calls a "static payment arrangement" or by obtaining mortgage advice and formally amending the term of the mortgage.

My understanding – and YBS should correct me if I am wrong – is that the static payment arrangement would not formally reduce the term of the mortgage. Rather, the monthly payments would not reduce. The impact of this along with the overpayments is that the mortgage would be repaid sooner than it would have a) without the overpayments and b) if the monthly payments were recalculated because of the overpayments.

YBS has not shown, however, that it explained in a clear, fair and not misleading way what Mr A and X needed to do to set up an overpayment where the term, rather than the payments, reduced. I am satisfied that Mr A and X wanted to use the static payment arrangement. But the email from YBS on 11 July 2016 did not just "lack clarity" – it contains incorrect information.

I say that as the email told Mr A and X that they would need to contact YBS's head office to set up the overpayment and they could do so by direct debit or standing order. YBS has now told us that it is unable to arrange a static payment arrangement where a standing order, rather than a direct debit is in place. That meant when Mr A and X phoned YBS in 2016 to set up the overpayments, they asked for a standing order to be set up. It followed that the overpayments were not working in the way that Mr A and X wanted.

The starting point for me is to put Mr A and X back in the position they would have been in had the mistake not occurred. So what would the mortgage look like now had the static payment arrangement been put in place? For the avoidance of any doubt, I think it would have been put in place had YBS communicated clearly.

I accept that Mr A and X will still have received the benefit of the overpayments. They were paying £600 a month in addition to the contractual monthly payment. They would still pay their mortgage off sooner than they otherwise would have had they not been making overpayments. They've also had the benefit of a reduction in the interest they've had to pay.

The other feature of the static payment arrangement was that monthly payments would not be recalculated because of the overpayments. To put it the other way, because Mr A and X were not benefitting from the static payment arrangement, each year YBS reviewed their monthly payments and recalculated them, taking into account the overpayment balance.

Effectively, this meant that Mr A and X were not reducing the term of the mortgage as much as they expected. As I said, they still had some benefit of the overpayments. But the recalculation meant that YBS was calculating the payments so that the reduced balance was paid off over the longer term. If the static payment arrangement was in place, Mr A and X would be overpaying as a result of the monthly payment too – the payments they would have made towards the capital each month would have been based on the original balance.

Of course, by reducing the monthly payment Mr A and X have made "saving" by paying less each month than they would have had the static payment arrangement been in place. But we have a longstanding approach to cases such as this where a mortgage has been underfunded due to an error by a mortgage lender. The starting point is for the lender to rework the account as if the mistake had not occurred. But I also need to consider when Mr A and X knew – or should have known – that the account wasn't operating as they'd expected.

I understand that the mortgage was Mr A and X's biggest financial commitment. They've also explained that overpaying to reduce the term was important because otherwise the mortgage would run past Mr A's intended retirement age. They were both reasons why it would have been reasonable for Mr A and X to check their annual mortgage statements. Even without those factors, I still consider there is a reasonable expectation that a borrower will check their annual mortgage statements.

If Mr A and X had done so, I can't see that the remaining mortgage term is included on the statements. And if my understanding is correct and the static payment arrangement had been explained to Mr A and X, they would not have been expecting the formal term of the mortgage to reduce in any event.

But the 2017 statement, issued in January 2018 says that they have a new mortgage payment and that payment was lower than they had been paying. So Mr A and X should have known that the arrangement they thought had been agreed was not in fact in place. Similar information is provided in later statements.

In March 2018, Mr A and X switched products. I note that the sales documents say that YBS did not give them advice for that transaction. The offer is for a term of 21 years and 2 months. But again, if the static payment arrangement was in place, that would not indicate a problem.

I accept that there were opportunities for Mr A and X to know that something wasn't right. They should have noticed their payments were going down and that could not be consistent with their understanding of the arrangement they thought they had.

On the other hand, YBS was the cause of the problem – and it has regulatory requirements to communicate clearly and fairly. I don't agree that there is no financial loss to Mr A and X because of what happened. I am satisfied they have paid less in capital than they otherwise would have had YBS treated them fairly. While they have made savings by paying less, there is no evidence that those savings are realisable. So Mr A and X are behind where they would have been had YBS acted fairly and reasonably.

I consider it would be fair for YBS to make up half the shortfall that has arisen as a result of its mistake. That takes into account that Mr A and X could have realised earlier there was a problem. I consider the redress should be calculated up to the point Mr A and X received new advice in 2021 and formally reduced the term of the mortgage. So YBS should:

- *Calculate what Mr A and X's mortgage balance would have been had a static payment arrangement been in place since the mortgage's inception and they made the full payments due on time – up until the new advice in 2021.*
- *Calculate the shortfall – that is the difference between the above amount and the mortgage balance as it was at the time of the 2021 advice.*
- *Apply half of the above amount to Mr A and X's mortgage as an overpayment. It should ask Mr A and X whether they wish to have this applied as a static payment arrangement.*

It is clear that Mr A and X have been caused distress and inconvenience as a result of this matter. They would have had the shock and upset of finding out their mortgage term had not reduced as they'd expected – along with the inconvenience of sorting this matter out. But I consider YBS's offer of £300 is fair for that. But the savings they have made are going to be more than £300. So I don't consider it fair to say that YBS should pay an additional amount to reflect any distress and inconvenience.

Mr A and X responded to make a number of points, including:

- YBS did not reduce the term of the mortgage in 2021. The shorter term is solely due to them taking out a new mortgage product. They made it clear that the 2021 application was not connected to their complaint and did not imply any acceptance of YBS's position. The term was not shortened by YBS.
- They were told by YBS that their payments would fluctuate over time – so they would not have thought that anything was amiss when there was a small variation in the monthly payment.

YBS responded to say, in summary:

- Neither a direct debit or standing order would formally reduce the term of the mortgage. That can only be achieved by receiving mortgage advice.
- If a direct debit was set up to collect overpayments then it would remain unchanged. Customers can also pay the contractual monthly payment by direct debit and have the overpayments collected by standing order. That meant when the contractual monthly payment went down, the standing order continued to pay the same amount of overpayment. So when the payment was reviewed annually the overpayments were slightly less. It was for the customers to review their overpayments after each annual review and ensure the monthly payment and overpayment "remains suitable" for their needs and to make sure the 10% annual overpayment amount is not exceeded. Mr A

and X failed to contact YBS upon each annual review to make the most of the overpayment allowance.

- It agreed that its email of 11 July 2016 could have been clear that is why it upheld the complaint and offered £300 compensation. The term would not formally reduce whether the was a direct debit or standing order set up.
- Mr A and X were under the impression that the term would formally reduce following overpayments. That was never the case and YBS never told them that.
- There was no mistake made. The information in the 2016 email could have been explained in more detail. At no point did YBS tell Mr A and X that the overpayments would be reflected as contractual change. By using the overpayments customers can reduce their balance more quickly, which will result in the mortgage being repaid before the contractual term. The confusion is with the term “reducing term”, which Mr A and X interpreted as contractually shortening the mortgage rather than informally ending their mortgage early.
- It was incorrect for me to say that it was a feature of the static payment arrangements that the monthly payment would not be recalculated because of the overpayments. All mortgages are subject to an annual review an neither the standing order or direct debit can change that. They are just different ways of managing the overpayments.
- YBS is satisfied that Mr A and X have benefitted by making overpayments in the way they did and the overpayments were fully considered while calculating the lower possible term reduction in 2021.

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.

I've reviewed everything again – and having done so I've reached largely the same conclusions I reached in my provisional decision. I note the points that YBS has made in response – and I will deal with that in more detail below – but I don't think that changes the outcome of this complaint.

The ability to make overpayments to reduce the term of the mortgage was clearly one of Mr A and X's stated needs when they took out the mortgage. YBS recommended a mortgage that had a facility that allowed overpayments and to reduce the mortgage term (albeit informally) by what it calls a “static payment arrangement” or by obtaining mortgage advice and formally amending the term of the mortgage. So the mortgage was suitable for Mr A and X.

YBS also had a duty to communicate with them in a way that was clear fair and not misleading. While the mortgage did have the static payment feature that was in line with Mr A and X's needs – that was no good if YBS did not explain properly how they could use that feature.

The 2016 email didn't explain YBS's policy in respect of overpayments correctly. YBS has confirmed that if a standing order was set up to make overpayments it would need to be adjusted annually. There is no evidence to show that Mr A and X were ever told this. I consider it more likely that they believed that by setting up a standing order they'd arranged the overpayments in line with their stated needs and circumstances – and had set up a static overpayment. YBS knew what Mr A and X's objectives were, so it never should have

suggested that they set up a standing order.

As I said in my provisional decision, I accept that under a static payment arrangement the term of the mortgage would not formally reduce. But clearly, if consistent overpayments were made each month, the mortgage would be repaid sooner than otherwise. YBS has highlighted that Mr A and X were under the impression the term would formally reduce. It said it never told Mr A and X this was the case. But I don't think this helps YBS. If it had explained the mortgage and the overpayment feature in a clear, fair and not misleading way then it is less likely that Mr A and X would have been confused about how it operated.

YBS said it was for Mr A and X to adjust the overpayment amount following the annual review of payments. I've already found there was no evidence that Mr A and X were ever told this by YBS. It was clearly an important feature of the mortgage for Mr A and X – it was one of their stated needs. Bearing in mind YBS's duty in giving advice to Mr A and X it would have been reasonable for it to show that it had brought this feature to Mr A and X's attention.

I am satisfied that making overpayments to reduce the term of the mortgage was an important objective for Mr A and X. I consider it likely that if YBS had explained how the overpayments worked in a clear, fair and not misleading way then Mr A and X would have either adjusted the standing order annually or set up a static direct debit instead. So they have lost out as they have made less overpayments than they would have had they received the correct information from YBS.

The starting point is to put Mr A and X in the position they would have been in had YBS acted fairly and had given them clear and accurate information about how the mortgage operated and what they needed to do to set up a static payment arrangement. If it had done so, I consider it is more likely than not that Mr A and X would have continued to make static overpayments at the level of the initial monthly mortgage payment. This was clearly an important objective for them. So they have lost out, as they have overpaid less than they otherwise would have.

In saying that, while I accept that Mr A and X might have expected some fluctuations in the payments, I think the changes went further than that – and they ought reasonably to have known that the mortgage was not operating as they expected at an earlier point. That is not to take away from the mistakes that YBS made in explaining how the mortgage worked and not making sure that Mr A and X had set up overpayments in line with their objectives. But YBS did send statements every year – and there was a reasonable expectation that Mr A and X would check them. If they had it would have been reasonable for them to see there was a problem.

I don't agree that there is no financial loss to Mr A and X because of what happened. I am satisfied they have paid less in capital than they otherwise would have had YBS treated them fairly. While they have made savings by paying less, there is no evidence that those savings are realisable. So Mr A and X are behind where they would have been had YBS acted fairly and reasonably.

I consider it would be fair for YBS to make up half the shortfall that has arisen as a result of its mistake. That takes into account that Mr A and X could have realised earlier there was a problem. I consider the redress should be calculated up to the point Mr A and X received new advice in 2021 and formally reduced the term of the mortgage. So YBS should:

- Calculate what Mr A and X's mortgage balance would have been had a static payment arrangement been in place since the mortgage's inception, in line with the original contractual monthly payments and they made the payments due in full and on time – up until the new advice in 2021.

- Calculate the shortfall – that is the difference between the above amount and the mortgage balance as it was at the time of the 2021 advice.
- Apply half of the above amount to Mr A and X's mortgage as an overpayment.

I accept Mr A and X's position that the advice in 2021 was unconnected to this complaint. But they knew the correct position at that point and it was for them to tell YBS what their needs and objectives were and to prevent any further loss. I can't see that they have complained about that advice or that it did not meet their needs and objectives. I don't see how I could reasonably say that the compensation should extend past the date of advice in 2021.

It is clear that Mr A and X have been caused distress and inconvenience as a result of this matter. They would have had the shock and upset of finding out their mortgage term had not reduced as they'd expected – along with the inconvenience of sorting this matter out. But I consider YBS's offer of £300 is fair for that. But the savings they have made are going to be more than £300. So I don't consider it fair to say that YBS should pay an additional amount to reflect any distress and inconvenience.

My final decision

My final decision is that Yorkshire Building Society should:

- Calculate what Mr A and X's mortgage balance would have been had a static payment arrangement been in place since the mortgage's inception, in line with the original contractual monthly payments and they made the payments due in full and on time – up until the new advice in 2021.
- Calculate the shortfall – that is the difference between the above amount and the mortgage balance as it was at the time of the 2021 advice.
- Apply half of the above amount to Mr A and X's mortgage as an overpayment.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr A and X to accept or reject my decision before 9 February 2023.

Ken Rose
Ombudsman