

The complaint

Mr and Mrs D complain through their representative that Lloyds Bank PLC trading as Scottish Widows Bank did not give them the full offset of their mortgage interest and restricted it to one part of the mortgage only. Mr and Mrs D say that as result they paid £10,000 more in interest than they should have.

What happened

Mr and Mrs D took a mortgage out with Scottish Widows which was arranged through a broker. The mortgage was to be an offset mortgage and Mr and Mrs D through their broker submitted an application for that based on borrowing of about £1,200,000. The assumed valuation of the property was £2,000,000 but in August the property was down valued to £1,600,000. The application was submitted on the basis that the mortgage was to be interest-only together with an application for the offset be applied to the interest on that. But after the down valuation in August, Scottish Widows required that only part of the mortgage was to be interest-only, for about £800,000, and the other part, for about £400,000 was on a capital and interest repayment basis. This was agreed in an email exchange between Scottish Widows and the broker and reflected in the mortgage offer dated 24 August 2020 and that was acceptable to Mr and Mrs D. The funds for the mortgage were released on 15 September 2020.

But because the mortgage was composed of two parts, although the same rate of interest applied to both parts, Scottish Widows' policy was to only apply the offset to one part. In the product brochure entitled "A Guide to Offsetting" at page 5 there is a Q&A section which contains a question relevant to this:

"Q. If my mortgage is made up of more than one rate or repayment method, can I offset against my total mortgage balance?"

A. No. You can only offset against one rate/repayment method – at application stage you'll need to choose which one."

Scottish Widows then applied the offset to the interest-only part although it didn't invite Mr and Mrs D or their broker to choose which part was to benefit as suggested in the booklet. Mr and Mrs D complained about the offset being applied to only one part of the mortgage, but they would have had difficulty exiting the mortgage as there was an early repayment charge applicable. That issue was resolved in May 2021 when the two accounts were merged, and Mr and Mrs D benefited from the offset over the total balance of the mortgage from that point. But the problem for Mr and Mrs D was that they lost the benefit of the offset interest that they believed they should have got from September 2020 until May 2021.

Our investigator's view

Our investigator didn't recommend that this complaint should be upheld. She felt that the bank had made the conditions of the mortgage reasonably clear and as this sale was conducted through a broker, it was the responsibility of the broker to explain the conditions to Mr and Mrs D.

Mr and Mrs D disagreed saying in summary that the condition of having one repayment type able to offset is hugely onerous and should be made clearer in the documentation and not hidden away as a question and answer in a 24-page booklet.

My Provisional Decision

I considered this complaint and as my view differed from that of our investigator I issued a Provisional Decision which I set out below:

“Mr and Mrs D took out this mortgage through a broker. Scottish Widows would have had little if any contact with Mr and Mrs D. Scottish Widows could offer a mortgage and, on certain products, the option of applying for an Offset Saver Account allowing the customer to offset their savings against the mortgage balance. The mortgage offer gives a general explanation to how this works and refers the customer to the product brochure for further details of how the offset facility works.

There appears to be two steps to applying for an offset mortgage. Mr and Mrs D through their broker apply for the mortgage and the broker submits an online form called Additional Mortgage Loan Details asking for the offset benefit to be applied to the mortgage. In this case the broker initially applied for a mortgage of about £1,200,000 all on an interest-only basis and submitted the Additional Mortgage Loan Details form online asking for offset to be applied to that interest-only mortgage. If the mortgage application was successful the offset would have been applied to all the mortgage.

But there was a problem with the valuation which meant that Scottish Widows wouldn't do all the mortgage on interest-only but, there had to be two parts, some £800,000 on interest-only and £400,000 on capital repayment. This had implications for the existing application for the offset benefit as, according to Scottish Widows policy, if the mortgage was composed of two parts only one part could benefit from the offset. Its Scottish Widows position, as stated above, that the broker should have been aware of this if they had read the product brochure.

It's fair to say that the broker proceeded on the assumption that the change to the composition of the mortgage hadn't affected the application for the offset benefit to apply to all the mortgage. Scottish Widows didn't tell the broker that the change in the accounts had affected its existing application to have the offset benefit applied to the whole borrowing.

From Scottish Widows point of view it had told the broker what would happen and fulfilled its duty by providing sales information, that if read, would have alerted the borrower as to what would happen if the mortgage was composed of more than one account. I understand the broker to be making the point that Scottish Widows in fact didn't give Mr and Mrs D the opportunity to choose which account would benefit, as the Q&A at page 5 of the product brochure suggests, with Scottish Widows choosing, without reference to the broker, the interest-only account as the one to gain the benefit of the offset. The broker says that this deprived Mr and Mrs D of the choice but also would have alerted them to the issue of the two accounts and that the offset benefit would apply to only one.

I raised this issue with Scottish Widows which responded as follows:

“The Broker has a Business Development Manager (BDM) assigned to him, and the BDM would be the point of contact if the Broker has any queries regarding any part of the Mortgage application, process or Offer. We do not contact the Brokers when an application is received as the keying process asks the Broker to select which part of the Mortgage the customer wishes to offset, so any queries regarding this matter should have been raised at this point. We have no record of this matter being queried at any point in the application process. See attachments. You can see from the application, the

Broker has keyed that the £800,000 has been selected to receive Offset benefit.”

Scottish Widows supplied me with a screenshot headed “Additional Mortgage Loan Details- All Applicants “which I supplied to the broker for comments. That is an application for offset where one account is ticked – the interest only account for £800,000 whereas the capital and interest account for £401,499 is unticked. At the bottom there is a further tick where the broker confirms his client had read and accepted the Offset Saver Terms and Conditions.

Mr and Mrs D’s broker said that it didn’t submit this document as presented to me. I’ve followed this up with Scottish Widows to understand what happened. My understanding is that when the broker submitted the original application, this form - Additional Mortgage Loan Details was also submitted requesting the offset facility to be applied to all the borrowing which was interest-only at that stage. Following the down valuation in August, Scottish Widows told the broker it couldn’t do it all on interest-only, but the borrowing needed to be split between interest-only and capital repayment. In August the broker on behalf of the clients accepted that.

But Scottish Widows didn’t tell the broker that the original application for the offset benefit to be applied to all the mortgage had to be revised and the broker wasn’t asked which part of the mortgage Mr and Mrs D wanted to benefit from the offset. The broker wasn’t asked to submit another Additional Mortgage Loan Details form detailing the two accounts and choosing which one as to benefit. Scottish Widows appears to have internally amended the original form without reference to the broker and presented it to us as if submitted by the broker. This purports to show the broker being made aware that Mr and Mrs D could choose to apply the offset benefit to one or other of the repayment mechanisms and the broker choosing the interest-only part to benefit.

I found the Additional Mortgage Loan Details form and the original explanation given to me by Scottish Widows to be misleading suggesting that the broker had the opportunity to consider this form and to have chosen the interest only part to benefit from the offset. But this form appears to have been amended in August without the broker’s knowledge.

What effect does this have on the complaint? Its Scottish Widows case that the broker should have known from reading the mortgage brochure booklet that if the mortgage was made up of more than one repayment method that the offset benefit applied to only one of those parts. But at the time Mr and Mrs D originally applied they were only applying for one payment method and completed and submitted the Additional Mortgage Loan details form on that basis.

The application changed in August after a down valuation and after an exchange of emails between the broker and Scottish Widows. Scottish Widows didn’t alert Mr and Mrs D to the fact that offset benefit which the broker had asked Scottish Widows to apply to all the mortgage, in the original Additional Mortgage Loan details document, would now only apply to one part of the mortgage. It seems to me that in these emails that it would have been reasonable to Scottish Widows to alert the broker to that significant change. That also could have been achieved had Scottish Widows, as it says it would do in the Product brochure, asked Mr and Mrs D to choose which repayment method they wanted to benefit from the offset. Scottish Widows failed to do this and failed reasonably to alert Mr and Mrs D that the offset benefit would not now apply to the whole mortgage. It also seems the me that the broker had only ever applied for the whole of the mortgage to be interest only – on the original form. That application remained outstanding in August when Scottish Widows simply amended the form without alerting the broker that it was doing so as if the broker had resubmitted a new form to meet the new situation. I consider that to be unfair.

I believe that Scottish Widows had ample opportunity to alert the broker to the fact that the

new application meant that Mr and Mrs D could no longer enjoy the benefit of the offset on all the accounts but by not doing so, misled the broker to understand that nothing had changed since the original application in respect of the offset. The process envisages the broker submitting a form – the Additional Mortgage Loan Details form – to allow the broker to request to which account the offset benefit applied. In this case the broker submitted a form based on there being only one account but when this changed the broker should have been asked or prompted either to submit a new Additional Mortgage Loan Details form reflecting the new situation or to agree to amend the original form. Neither of these reasonable steps was taken by Scottish Widows but Scottish Widows amended the original form as if submitted by the broker but without its knowledge or authority.

My intention is to uphold this complaint. As Mr and Mrs D were deprived of the offset benefit which they had been led to believe was available to them, Scottish Widows should, as compensation, rework the mortgage as if the offset benefit had been applied to all parts of their mortgage from September 2020 until date of settlement. Scottish Widows should make sure the mortgage balance is the same as it would have been had the offset benefit been applied in that way from September 2020. In addition, for their distress and inconvenience, Scottish Widows should pay Mr and Mrs D £500.”

I set the above out as my Provisional Decision and invited submissions from Mr and Mrs D and from Scottish Widows. I received a further submission from Scottish Widows but not from Mr and Mrs D. Scottish Widows had revised its view of this complaint and I set this out below

“Our Position:

- *The Broker submitted the original application in a way which meant the whole of the mortgage balance would benefit from offsetting*
- *Based on the lower valuation, we explained to the Broker that we would not offer the whole of the balance to be repaid on an Interest Only basis, however, we could offer on a part IO and part capital repayment (C&R) basis*
- *As it was agreed the customers would proceed on the part IO and part C&R repayment basis, **the Bank proceeded to amend the application accordingly***

The Bank made the changes to the application:

- *I want to clarify that once a Broker submits their original application, any changes to that application are made by the Bank*
- *The Broker doesn't have the access or facility to amend the original application. I'm sorry if it was ever intimated in any way that the Broker amended the application as this is clearly not the case*
- *The Bank accept full responsibility for the changes made to the application*
- *The system will automatically select the IO part of the mortgage to offset when any changes are made, as the IO part will benefit the most from offsetting*
- *I agree we should not have proceeded at this stage without discussing the offsetting with the Broker*

Missed opportunity

- *You quite rightly pointed out that it is the customer who should make the decision on which part of the mortgage they wish to offset against*
- *I agree we should have contacted the Broker in respect of the change to the mortgage being split into two parts to ensure they were aware of the implications of the change and to find out which part the Broker / customer would like to offset against*
- *This would've given the Broker / Customers the necessary information to make an informed choice on how they wished to proceed at this point*

Taking everything into consideration we agree to reconcile the account as suggested and make the payment of £500.00 for the upset and disappointment caused."

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 welcome Scottish Widows further investigation and that it was able to come to a conclusion agreeing with my Provisional Decision. Scottish Widows did ask me to review a part of my decision as it says that it did not deliberately "*mis-lead*" the customer or the broker. I refer to the broker being misled and myself being misled a number of times in my Provisional Decision. For my own part, I said that during my investigation that a document - the Additional Mortgage Loan details document with a tick for a partial offset - was presented to me with an explanation that it had been altered by the broker which it had not. This was misleading and required further investigation before I could conclude that the broker hadn't altered the document. But, I accept that it wasn't deliberate but more likely through a misunderstanding of how the process worked.

I also said that "*Scottish Widows had ample opportunity to alert the broker to the fact that the new application meant that Mr and Mrs D could no longer enjoy the benefit of the offset on all the accounts but by not doing so, misled the broker to understand that nothing had changed since the original application in respect of the offset.*" Again, I don't say its deliberate but a result of a process which Scottish Widows confirmed was inadequate that led the broker to understand that the offset benefit would be applied to the whole mortgage as originally envisaged. So, I don't accept that my Provisional Decision contains any inaccuracy that requires amendment.

In the light of the acceptance of my Provisional Decision by Scottish Widows and my further review of the evidence I believe that my Provisional Decision represents a fair outcome to this complaint and I will be upholding this complaint on the terms set out in that decision.

Putting things right

I require Lloyds Bank PLC trading as Scottish Widows Bank to rework the mortgage as if the offset benefit had been applied to all parts of Mr and Mrs D's mortgage from September 2020 until date of settlement. Scottish Widows Bank should make sure the mortgage balance is the same as it would have been had the offset benefit been applied in that way from September 2020. I also require Scottish Widows to pay Mr and Mrs D £500.

My final decision

My decision is that I uphold this complaint and I require Lloyds Bank PLC trading as Scottish Widows Bank to pay compensation as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr D and Mrs D to accept or reject my decision before 21 February 2023.

Gerard McManus
Ombudsman