

The complaint

Mr S complains that NRAM Limited were lending irresponsibly when they offered him four buy-to-let mortgages on interest only terms. He also complains about the interest rate charged on the mortgages and his inability to re-mortgage on a lower interest rate.

What happened

In 2007, Mr S took out four buy-to-let mortgages with Northern Rock after receiving advice from a broker. All four mortgages were taken out on interest only terms over 25 years.

The first offer issued in March 2007 confirmed an initial fixed rate of 5.29% would apply to the mortgage until 1 March 2009, after which, the mortgage would revert to the standard variable rate (SVR) for the remainder of the term. At that time the SVR was 7.34%.

The next two offers issued in April 2007 confirmed an initial fixed rate of 5.29% would apply to each mortgage until 1 May 2009, after which, the mortgages would revert to the SVR for the remainder of the term. At that time the SVR was 7.34%.

The fourth offer issued in July 2007 confirmed an initial fixed rate of 5.99% would apply to the mortgage until 1 September 2009, after which, the mortgage would revert to the SVR for the remainder of the term. At that time the SVR was 7.84%.

During the 2008 financial crisis, Northern Rock was nationalised to avoid collapse of the bank. NRAM was later formed to manage most of the remaining Northern Rock mortgages, which included Mr S' mortgages – where they remain to date. For ease, I shall refer to NRAM for the remainder of this decision.

In January 2020 Mr S complained to NRAM about the sale of the mortgages. He complained that the mortgages were lent to him as a result of risky lending practices. Since the financial crisis, the properties have been in negative equity. He hasn't made a profit on any of the properties but has been unable to re-mortgage or sell the properties without leaving a shortfall, which he doesn't have the means to repay.

He also complained about the interest rate charged on the mortgages to date. He said that as a result of unfair terms, the SVR has been excessively high over the years despite interest rates generally being at record low levels. Mr S also made a complaint to the broker that sold him these mortgages.

NRAM responded to Mr S' complaint in February 2020. It didn't uphold the complaint. Mr S asked our service to consider his complaint, but NRAM didn't give our service consent to consider the complaint about events that took place more than six years ago.

An investigator at our service looked into things and agreed Mr S' complaint about the sale of the mortgages had been made too late. He also said that our service could only consider Mr S' complaint about the interest rate charged in the six years leading up to his complaint, so from January 2014 onwards. He didn't think the complaints brought out of time had been made late as a result of exceptional circumstances. The investigator looked into Mr S'

complaint about the interest rate charged on his mortgages since January 2014, but he didn't think NRAM had acted unfairly.

Mr S disagreed with the outcome the investigator reached. He explained that he didn't know he had a reason to complain until he received advice from a solicitor, and carried out a Data Subject Access Request where he received information about his mortgages. He said it was only then that he realised his position was a result of poor lending practices. He also said he was not aware there was a problem with the way the SVR was set until his solicitor pointed this out to him, which wasn't until 2019. He said until then, he thought he'd just made bad investment decisions and didn't realise he had a cause to complain against the lender.

The investigator wasn't persuaded to change his mind, so the complaint was passed to an Ombudsman to decide what we can and can't consider.

The Ombudsman issued her decision in February 2022 explaining that our service only has the power to consider Mr S' complaint about the interest rate charged from January 2014 onwards. She was satisfied that any complaint about events that occurred before this date - including how the mortgages were sold and the interest rate charged before this date - had been made too late. The Ombudsman explained that when considering Mr S' complaint about the interest rate charged from January 2014 onwards, we'll need to take account of the impact of what contributed to those charges - including things that happened before that time which influenced the rate charged at that time.

The case was passed back to the investigator for him to carry out a revised assessment into the part of Mr S' complaint that was made in time. The reason for this is that, since the investigator first considered the complaint, our service has received further detailed information from NRAM about how it varied its SVR. So, the investigator considered this information in relation to Mr S' case to ensure he'd given everything full and fair consideration. In doing so his opinion remained the same - as he didn't think NRAM had acted unfairly in the way it varied the SVR from 2014 onwards.

Mr S remained unhappy and asked for his case to be decided by an Ombudsman. As explained, another Ombudsman has already issued a decision that sets out what our service can and can't consider. As such I won't be revisiting the matter of our jurisdiction again. My decision focuses on the merits of Mr S' complaint - that being whether NRAM has treated him fairly from January 2014 onwards - the period which falls into our service's jurisdiction.

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.

In considering what is fair and reasonable in all the circumstances of Mr S' complaint, I am required to take into account: relevant law and regulations; regulators' rules, guidance and standards; codes of practice; and where appropriate, what I consider to have been good industry practice at the relevant time.

I've given careful consideration to all the submissions made by both parties, but I won't address each and every point that has been raised. I'll focus on the matters that I consider most relevant to how I've reached a fair outcome - in keeping with the informal nature of our service.

Having done all that, I don't think this complaint should be upheld. I realise that will be disappointing for Mr S. But I hope the reasons I have set out below will help him to understand why I have come to this conclusion.

The part of Mr S' complaint that our service can consider largely centers around him being overcharged interest on his mortgages and him not being able to obtain a lower interest rate with NRAM. Mr S says these issues have put financial pressure on him and will impact his ability to repay the mortgages at the end of their term.

I'll address these issues in turn starting with whether NRAM treated Mr S unfairly by not offering him a new interest rate on his mortgages.

Mr S' mortgage offers made it clear that once the fixed interest rates ended in 2009, the mortgages would revert to the SVR, and this in fact happened. Neither the mortgage offers nor the mortgage terms and conditions say that NRAM has to make another fixed rate available after the initial ones ended, or that it has to offer Mr S any rate other than the SVR.

This means that Mr S' mortgages have operated as the contracts said they would, on the terms he agreed to when he borrowed the funds in 2007. And there's nothing beyond the mortgage terms which says NRAM has to offer new rates either – there's no law, or rule of mortgage regulation, which says that a lender has to offer new rates to existing customers.

During the period in question that this decision relates to, from May 2014 onwards, NRAM has not offered new rates to any existing customers. So Mr S has not been treated any differently to other NRAM customers and his mortgages are operating as they should have done according to its terms and conditions.

That leads me to consider whether the SVR Mr S was charged during this period was fair. In answering this question, I am doing so in the context that this complaint only concerns the fairness of interest charged to Mr S' mortgages in the six years leading up to his complaint – so from January 2014 – for the reasons I've given.

However, in order to consider the fairness of the interest Mr S' was charged during the period that is in time, it's necessary for me to consider historic changes to NRAM's SVR. This is because the SVR charged from January 2014 is the result not only of decisions NRAM made during that period, but also the result of decisions it made prior to it. But, in the event I were to award any redress, I would only be able to award for the period that is in scope of this complaint – January 2014 onward.

To assess the fairness of the interest rate terms, it is helpful to first set out the relevant terms themselves. In addition to the terms in the mortgage offers that I've already set out, I've also considered what the supplementary mortgage conditions say about how the SVR on Mr S' accounts would operate.

The Mortgage Offer General Conditions (2005) set out:

***"Standard Variable Rate** means such rate as we from time to time decide to set as the base from which to calculate Interest on our variable mortgage loans (disregarding the restrictions on what we can charge under condition 7 of the Offer). The current Standard Variable Rate which applies to your Loan is set out in the Offer. We may change this rate from time to time under Condition 7 of the Offer. If we transfer or dispose of the Offer, the person to whom we make the transfer may change the rate to its own base rate which applies to its variable rate mortgage loans. That rate will then be the Standard Variable Rate under the Offer and the person to whom we make the transfer may make further changes to that rate under condition 7 of the Offer."*

"7. Changing the Interest Rate

7.1 We may reduce the Standard Variable Rate at any time.

7.2 We may increase the Standard Variable Rate at any time if one or more of the following reasons applies:

- (a) there has been, or we reasonably expect there to be in the near future, a general trend to increase interest rates on mortgages generally or mortgages similar to yours;*
- (b) for good commercial reasons, we need to fund an increase in the interest rates we pay to our own funders;*
- (c) we wish to adjust our interest rate structure to maintain a prudent level of profitability;*
- (d) there has been, or we reasonably expect there to be in the near future, a general increase in the risk of shortfalls on the accounts of mortgage borrowers (whether generally or our mortgage borrowers only), or mortgage borrowers (whether generally or our mortgage borrowers only), whose accounts are similar to yours;*
- (e) our administrative costs have increased or are likely to do so in the near future”*

NRAM has told us that it relied on Condition 7.1 for all its reductions to the Bank of England base rate (“base rate”). In 2018 the SVR did increase following increases to the base rate. NRAM has said that it relied on Conditions 7.2 (a) & (b) to make these changes.

I’ve carefully considered the above Conditions and I’m not satisfied that all the terms are sufficiently transparent. While grammatically easy to follow, the relevant terms allowing for the SVR to be varied are broad, and the circumstances in which changes might be made give NRAM significant discretion about when it can make changes to the SVR and by how much.

I think some of the terms are wider than reasonably necessary to achieve a legitimate purpose and are so subjective that they don’t all clearly explain to the consumer when a change may be made or the method for determining the new price. In my opinion it would be difficult for a customer to understand the basis and the mechanics for any decisions taken that relied on these terms, or to be able to understand the economic consequences of entering into the agreement and, if necessary, to challenge a variation made in reliance on them. That means that there’s a real possibility a court would consider there to be unfair terms within the Unfair Terms in Consumer Contracts Regulations (UTCCR), which is the relevant law for me to take into account.

Having reached this conclusion, I also need to consider whether – at the time the contract was taken out – there were likely to be such significant barriers to Mr S dissolving the contract that he could not effectively make use of the right to do so. If there were such barriers, that may mean that the variation terms are unfair.

In assessing whether the terms are unfair - the test is not whether there were significant practical barriers for Mr S at the point at which his interest rate was varied, but rather whether it was foreseeable at the time the contracts were entered into that there may have been such barriers.

There was no ERC applicable to Mr S’ mortgages at the point they reverted to the SVR in 2009. So, if NRAM had exercised its rights as set by the variation term, and Mr S was unhappy with that decision, he was free under the contract to transfer his mortgages to

another lender should he have wished without having to pay this charge.

Mr S has said that since the financial crisis, his properties have been in negative equity. As such he has been unable to re-mortgage or sell the properties without leaving a shortfall, which he doesn't have the means to repay. I do empathise with Mr S' circumstances. But I don't think the downturn in the global economy was predictable; or that it was reasonably foreseeable at the time the contracts were entered into that Mr S may struggle to refinance his mortgages in the future; or that this would pose a real and practical barrier to Mr S dissolving his mortgage contracts with NRAM.

That said, for the reasons I've explained, I do consider that there is a reasonable basis to conclude that the variation terms are overly broad and do not explain adequately the mechanism for determining the new price. Whilst so, the central issue I must consider is whether there has been any unfairness to Mr S from January 2014 onwards. The fairness of the underlying variation clause will not of itself properly answer that question.

Under our rules, we are required to consider what is fair and reasonable in all the circumstances. That includes – but is not limited to – relevant law. So, while I have taken account of the relevant law regarding unfair contractual terms, I've also thought more broadly about whether the way the terms have been used has resulted in Mr S being treated unfairly. That is the ultimate question I need to answer when weighing up if Mr S' case should be upheld.

Firstly, I must point out that there isn't anything inherently unfair about a mortgage reverting to the SVR. They serve a legitimate purpose in permitting lenders to provide for future changes that justify changes in the rate, where costs to them are variable. Some borrowers choose to pay the SVR on their mortgage as a result of the flexibility it offers.

Saying that, I need to look at how the SVR has been varied both before and after January 2014, and having considered all the available evidence, I am not persuaded NRAM has varied the rate unfairly. I have set out why below.

Between 2007 (when Mr S took out his mortgages) and April 2009, the SVR only reduced. But the difference between the SVR and the base rate increased from 2.09% to 4.29%.

These were not tracker mortgages, so NRAM was not contractually obligated to track the base rate. Nor is it the case that Mr S' mortgage had a 'cap' preventing NRAM's SVR from increasing beyond a certain 'margin' above base rate.

NRAM has provided us with evidence to show how it reviewed the SVR over the relevant period, the decisions it took when it came to varying the rate and by how much, as well as its general commercial strategy at the time. For reasons of commercial confidentiality, I haven't set out the evidence provided by NRAM in full or provided copies of it to Mr S. Our rules allow me to accept information in confidence, so that only a description of it is disclosed, where I consider it appropriate to do so. In this case, I do consider it appropriate to accept the information and evidence NRAM has provided in confidence, subject to the summary of it I have set out in this decision.

During this time, the mortgage market was going through a period of significant change as a result of the global financial crisis. This impacted the funding costs of businesses and was reflected in changes to a number of lenders' interest rates charged across the market at the time. This was clear at the time and has been the subject of analysis by both the Bank of England and the FCA since. Whilst the base rate did reduce significantly during this period, the cost to lenders of funding their businesses changed, as did their prudential requirements. These were made up of several factors that are not directly linked to base

rate. There was a substantial risk to all lenders during this period and they all had to find ways to mitigate that risk while balancing the need to treat customers fairly.

NRAM has told us that, like many lenders at the time, it was predominantly funded by wholesale funding. The cost of which was in the most part, contractually defined by reference to LIBOR and LIBOR generally followed base rate prior to the financial crisis. As a result, changes in base rate tended to result in changes to cost of funding. Before the financial crisis, changes in costs of its retail funding also tended to correspond to changes in base rate.

However, during the financial crisis, there was a significant dislocation between LIBOR and base rate, such that reductions in base rate were not matched by commensurate reductions to LIBOR or to NRAM's cost of wholesale funding. In addition, access to wholesale funding became harder to come by as lenders became more concerned at the risk of default - NRAM in particular has shown how its credit rating was impacted and the implications this had on its ability to raise funds and the cost of its funding. It also experienced an outflow of its retail savings deposits following negative press in late 2007.

To avoid collapse, NRAM received State Aid in the form of a Government loan in September 2007. With the aid came several conditions on how NRAM could operate and obligations on how and when it should look to repay the loan. Understandably, this significantly impacted its commercial strategy and with it, the cost of funding mortgages like Mr S'. To add to this, NRAM was nationalised in February 2008 with its entire share capital being transferred to HM Treasury. One of the conditions of the restructure was that NRAM would be limited to a maximum 1.5% share of all retail funding in the UK and 0.8% in Ireland.

In addition, as part of its restructure, it was agreed NRAM would transfer all its higher quality assets to a third party, whilst the lower quality assets would remain with NRAM and be wound down. Given the perceived 'quality' of its remaining assets, this had a further impact on the cost of NRAM's funding.

NRAM reduced its SVR on several occasions during this period, just not by the same proportion as the base rate. Given the documented increase in cost of funding across the industry, including for NRAM specifically, and the obligations surrounding the Government loan, I am satisfied NRAM balanced its own financial position and obligations at the time with the impact such changes would have on customers like Mr S.

And while NRAM's SVR was at the higher end of what was being charged across the industry at the time, it was not an outlier, with several lenders charging a higher SVR. While the SVR charged by other lenders is not directly relevant to NRAM's cost of funds, these factors reassure me in my conclusion that NRAM's decisions on how much to reduce its SVR by were proportionate to the costs it - along with the rest of the industry - faced at this time and not unfair.

I have not seen any evidence to suggest the changes it made were arbitrary, excessive, or unfair. Rather, the evidence I've seen satisfies me that NRAM acted to protect its legitimate interests while balancing its obligation to treat Mr S fairly. And I'm further satisfied that the evidence NRAM has provided is corroborated by evidence of wider market conditions at the time.

Summary

Overall, taking into account all of the changes made to the SVR, while the terms do provide NRAM with wide discretion in regard to when or whether to vary the SVR charged on Mr S' mortgages, I don't think there is anything to suggest that it has acted unfairly or

unreasonably, or that Mr S has overpaid interest as he claims.

Finally, I note that Mr S is unhappy that NRAM won't agree to his proposals to voluntarily surrender his properties. In these circumstances and due to the nature of the proposals put forward by Mr S, it is NRAM's discretion whether it agrees to such proposals. In this case, I have not concluded that NRAM has got things wrong and so I don't expect it to take any action to put things right. As such, I can't reasonably direct NRAM to accept the proposals in these circumstances.

My final decision

My final decision is that I don't uphold this complaint as such I don't expect NRAM Limited to take any action in response to this complaint.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr S to accept or reject my decision before 25 August 2023.

Arazu Eid
Ombudsman