DRN-4225694

The complaint

Mr and Mrs S complain about their second charge mortgage (secured loan) with Blemain Finance Limited trading as Together. They're unhappy that their mortgage balance has increased and think Together isn't treating them fairly in threatening repossession. And they say they were unaware that the mortgage was taken out on interest only terms.

What happened

Mr and Mrs S took out a second charge mortgage with Together in December 2006. They borrowed around £46,000 (including fees) over 25 years.

Since then Mr and Mrs S have struggled with the loan and repayments and it's been in arrears for long periods. In 2022, Mr and Mrs S complained about the loan balance and about how Together had treated them.

Mr and Mrs S say that they were unaware the loan was taken out on interest only terms. They say they've paid over £70,000 over the years – yet the balance is still higher than the original borrowing. They say the loan was irresponsibly lent, including because Mr S was disabled and restricted in his ability to work when the loan was taken out. Mr and Mrs S are struggling with the monthly payments. Together has offered to assist them with selling the property, but they don't want to do that. Mr S continues to be unwell, and they say the loan and their problems with it are having an adverse effect on both their mental health.

Together said any complaint about the sale of the loan or the circumstances in which it was lent was out of time. It said the mortgage balance was correct, and it had increased because of extra interest applied when payments were missed or made late. Together said it had wrongly applied £509.20 of fees relating to buildings insurance, and it refunded those fees together with interest of £1,654.23 to reduce the loan balance. It said it had applied other fees and charges to the loan balance, but they had been correctly applied in accordance with the terms and conditions. But it said that it hadn't always done enough to make sure Mr and Mrs S were aware of the impact of not making payments by their due date on the amount of interest they were charged, and it refunded a further £587.68 in additional interest. And it offered £150 compensation for delays in dealing with their complaint.

Together told Mr and Mrs S that because of additional interest and fees and charges, their balance had increased. It said that for their loan to be paid off by the end of the term, they would either need to pay a lump sum of around £23,000 to reduce the loan balance to what it ought to have been, or increase their monthly payments to around £750. Mr and Mrs S say this is not affordable.

Our investigator didn't recommend that the complaint should be upheld, so it came to me for a final decision to be made. I reached a different view, so I issued a provisional decision to allow the parties to have a further chance for comment before I make a final decision.

My provisional decision

I said:

The sale of the loan

There are limits on what I can consider as part of this complaint. Because of when the loan was taken out, and how much was borrowed, this is an unregulated loan. That means it isn't covered either by the mortgage rules or by the Consumer Credit Act.

Until 1 April 2014, the Financial Ombudsman Service could only consider complaints about Together relating to loans covered by the Consumer Credit Act. The rules changed on 1 April 2014, and since then we've been able to consider all Together's lending, regulated or not. But because this is an unregulated loan, we can only consider things that have happened since 1 April 2014, not things that happened before that.

Secondly, there are time limit rules that apply to complaints. A complaint must be made within six years of the date of the event complained of – or, if that gives more time, within three years of the date the complainant knew or ought reasonably to have known of cause for complaint. Where a complaint is about matters older than that, a firm is entitled to refuse to consent to us looking at those things, and that's what Together has done here. I understand Mr and Mrs S don't think that's fair, but under the rules Together is entitled to withhold consent. We can however consider things that happened out of time if there are exceptional circumstances that explain why a complaint couldn't have been made in time.

What all that means is that anything that happened before 1 April 2014 doesn't fall within the jurisdiction of the Financial Ombudsman Service at all. And for things after that date, we can only consider them if the complaint was made in time.

We cannot therefore consider the lending decision, or whether Together lent responsibly, because that happened in 2006. But we can consider how Together treated Mr and Mrs S in the six years leading up to their complaint. I don't think the three year rule gives Mr and Mrs S more time, since they would have known of their difficulties at the time, and Together sent them regular statements showing the fees charged and how the balance was growing. And while I'm sorry to hear of the health difficulties and other problems Mr and Mrs S have experienced, I don't think they amount to exceptional circumstances that prevented them complaining sooner than they did, because I can see they were in regular contact with Together and so could have complained if they'd decided to do so.

For all those reasons, in this decision I'll focus on how Together has treated Mr and Mrs S since 3 August 2015, which is six years before they first contacted Together about this complaint.

The nature of the loan

I will just address one issue, though. Mr and Mrs S say they've only recently discovered that this is an interest only loan, and that should have been made clear to them from the start.

But this isn't an interest only loan. It's a repayment loan – meaning that, if Mr and Mrs S had managed to keep up with all their payments and Together hadn't added any other fees, the loan would be paid off by the end of the term in early 2032.

But Together has added various fees and charges over the years (though it's since refunded some of them). And Mr and Mrs S have missed many payments, or made *others late, over the years.*

If the loan was on track, each month Mr and Mrs S would pay enough to cover that month's interest, plus also repay some of the capital. If they miss a payment, however, they don't pay off the interest and instead it gets added to the loan balance. And they also don't pay off any of the capital. That means that next month the balance is higher – and so they are charged more interest. Unless they pay off that extra interest as well as the regular monthly payment, the balance will stay higher, and they will be charged more interest, each month after that too.

Where multiple payments are missed, even if they're made up later, the result is that this extra interest can significantly increase the loan balance. And where fees are added to the balance, interest is charged on them too – which has the same effect.

But the monthly payment Mr and Mrs S are charged each month is based on the original loan profile – in other words, the amount it was calculated at the start they'd need to pay each month to clear the loan. Because the balance has increased in the meantime, that payment is no longer enough.

In fact, the situation Mr and Mrs S are now in is that the missed payments over the years, plus the fees, have had such an impact on the loan balance that the interest charged each month is more than the contractual monthly payment. Even if Mr and Mrs S made their required payment in full, the balance at the end of the month would still be higher than it was at the start.

So this is not an interest only loan. It never was. It's a repayment loan. But the balance isn't reducing each month – in fact, it's going up – because of the impact of past missed payments and fees.

That's why Together told Mr and Mrs S that to get the loan back on track and pay it off by the end of the term, they'd need either to pay a lump sum of £23,000, or increase their monthly payments to £750. At that point, the loan balance was £23,000 higher than it should have been because of the missed payments , fees and additional interest. To get things back on track, Mr and Mrs S would need to pay that amount to reduce the balance to where it should be. Or, rather than paying that amount as a lump sum, they could increase their monthly payments to £750 a month for the rest of the term.

Whether that was a fair thing for Together to ask them to do is something I'll come on to shortly. But I first wanted to set out the facts and reasons behind why the loan was in that position and why Together said what it did, prompting Mr and Mrs S to complain.

<u>Fees and charges in 2016</u>

In its response to Mr and Mrs S's complaint, Together agreed to remove a substantial amount of fees, mostly related to insurance charges in the early days of the loan. As I've explained, I can only look at things since August 2015.

Since then, Together has applied arrears charges of £50 in November and December 2016, January and February 2017, and monthly since April 2022.

Mr and Mrs S had arranged a payment plan in July 2016. They were in around £4,000 of arrears at this time. They agreed to pay their regular monthly payment of around £440, plus an additional £70 to reduce the arrears. Mr and Mrs S kept to this *for the next few months. But in November they didn't make a payment.*

Together tried to contact Mr and Mrs S without success a few times, but managed to speak to them on 29 November 2016. Mrs S explained that she'd been in hospital and had reduced income as a result. She made a card payment of £500 (which cleared on 1 December) and agreed a new payment plan of £60 above the monthly payment from January 2017.

Payment was due on 5 January 2017, but Mr and Mrs S didn't make payment until 14 January. A new payment plan was agreed on 30 January, with the first payment due by 5 February and then monthly thereafter. Mr and Mrs S made a further payment on 31 January and then again on 1 March.

It was fair to charge an arrears fee in November, since Mr and Mrs S didn't make a payment and Together tried to contact them and agree a new arrangement. However, they did make payments on 1 December, 14 January and 31 January (for February), in each case for more than the monthly payments. I'm not persuaded it was fair to charge arrears fees in those months, and I think Together should refund those three fees, as well as interest charged on them.

<u>The account since 2016</u>

For some time Mr and Mrs S kept to the payment arrangement. They were paying around £500 a month, and as interest charged was around £460, the balance was gradually reducing, though not by enough to have paid it off within the existing term. At this time, interest was around £460 a month, so the capital was reducing by around £40 per month.

In August 2018 Mr and Mrs S missed a payment, and they only paid £50 in June and July 2018. But other than that, they kept to the arrangement until May 2020.

Mrs S contacted Together in May 2018, explaining that she was experiencing health problems and was trying to keep working even though her doctor recommended she didn't. Mr S was disabled and unable to work throughout this period. Together agreed a payment arrangement of £50 for June and July. Mrs S next spoke to Together in late August. She said it was a struggle but she would try to maintain the previous arrangement of £500 per month.

Mr and Mrs S missed payments due in May, June, July, August and September 2020, then resumed making payments in October. But from October onwards, they only paid around £450 per month - £10 more than the interest being added. Mr and Mrs S maintained these payments until May 2021, after which they made no further payments before their complaint apart from a one-off sum of £200 in March 2022. Together didn't charge arrears fees in 2020, but charged £50 per month from April 2022.

In May 2020, Mrs S contacted Together by email to say she was off work and didn't feel able to talk about her circumstances. Together agreed a coronavirus payment deferral for three months, and then a further month in August 2020 when Mrs S explained she had only recently returned to work and wasn't yet receiving full pay.

In May 2021, Together froze interest for two months following receipt of a breathing space request. Mrs S had lost her job. In September 2021 she got another job, but paying less than she'd earned before, but then she took time off sick for a medical procedure. Together agreed a nil payment arrangement. In January 2022 Mrs S *offered to resume paying £500 per month but Together asked to go through their income and expenditure before it would agree. Together then said that £500 wasn't enough to ensure repayment of the loan and the payment would need to be increased to over £700 per month. It suggested Mr and Mrs S seek advice about how to "exit" from the loan.*

Throughout this period, Mr and Mrs S have been in regular contact with Together. They've given it details about their finances and wider situation. Mr S is disabled, in receipt of benefits and not able to work. Mrs S has been working, but has her own health issues and has been out of work for periods.

I think the evidence is clear that Mr and Mrs S have been doing their best to keep up to date with the loan, paying what they can when they can.

However, it seems that they've been unable to afford to pay more than £500 per month even when Mrs S is working, and at times have struggled to pay that.

Together was right that as things stood in 2021 and 2022 Mr and Mrs S were unlikely to be able to repay the loan balance. Even if they could maintain the payment of £500 per month, that would cover the interest, but make very little reduction in the capital.

Together advised Mr and Mrs S that they'd need to increase their monthly payments to over £750 to ensure the loan was paid off by the end of the term. It's clear they weren't able to do that, so Together suggested they get independent financial advice to consider "exiting" the loan – which presumably means selling their property to repay it, since there was no other way they could do so.

I've reviewed everything that happened over this period, including the other contact between Mr and Mrs S and Together at times when they were keeping to the various arrangements (which, for reasons of space, I haven't detailed above).

I think Together did take steps to assist Mr and Mrs S, as I'd expect. It's agreed a series of payment arrangements and on particular occasions offered forbearance where Mr and Mrs S have struggled to make individual payments. This is what I'd expect it to do.

However, I think there's more Together ought to have done. It ought, acting fairly, to have taken a step back and looked at Mr and Mrs S's situation in the round. Together has correctly identified that Mr and Mrs S are not on course to repay the mortgage by the end of the term, and in fact were not making substantial in-roads into the capital even when they were making payment.

It's clear from their circumstances that Mr and Mrs S were paying what they could, and are unlikely to be able to pay any more at any time in the future either.

Together's only response to this was to suggest that Mr and Mrs S consider "exiting" the loan – selling their property to repay. It didn't consider other ways in which it could have assisted.

In my view, acting fairly, Together ought to have done so. It would have been fair and reasonable for it to look at the loan balance, look at what Mr and Mrs S were paying and what they could afford to pay, and think about whether they were on track to clear the balance – or whether, in fact, their situation was not improving and risked getting worse as the remaining term got shorter without the balance reducing. And, if *so, what could be done to get things back on track.*

Freezing interest in situations like this – that is, reducing the interest rate to 0% - is a relatively common form of forbearance in the second charge lending market, in my experience. In the right situation, doing so can amount to good industry practice.

In this case, Mr and Mrs S had been paying around £500 per month for several years. That was the most they could afford – and at times even that was a struggle. Their loan balance was not significantly reducing, even as the time left on the loan shrank. In that situation, I'd expect a responsible lender acting fairly to review the loan balance, check to see whether the loan was on track to be repaid by the end of the term – and, if not, consider what action needed to be taken in light of the borrower's financial situation at that time. Actions might include amending the monthly payment, extending the term, or reducing or freezing the interest. But Together didn't consider any of these options – it merely suggested Mr and Mrs S might want to think about selling the property. I don't think that was fair and reasonable, as it put the entire onus on Mr and Mrs S and didn't involve Together thinking about what it could fairly do to assist them.

Taking into account Mr and Mrs S's financial and health situation in 2021, there should have been a review of the account – with a view to showing the necessary forbearance to allow Mr and Mrs S to clear the loan balance in an affordable way by the end of the term. Doing so would need to take into account Mr and Mrs S's circumstances at the time as well as the history of the loan and reasons why it was in the position it was in.

I'm satisfied that Together ought, acting fairly and reasonably, to have frozen – stopped applying – the interest, so that Mr and Mrs S could focus on reducing the capital balance by the end of the term. I've reviewed the history of the account, and I think that decision ought fairly have been taken by the end of 2020 – when Mr and Mrs S had come off a coronavirus payment deferral, but Mrs S had lost her previous job and was experiencing further health concerns which would impact their ability to make payments in the future. It was clear to Together by this point that it was unlikely Mr and Mrs S would be able to repay their loan, and so it ought to have thought about what further action it could take to assist them.

To put matters right, therefore, Together should re-work the account as if it had reduced the interest rate to 0% from 1 December 2020. Any payments Mr and Mrs S have made since then should be used to reduce the capital balance of the loan.

Together should also remove any arrears fees it has charged during the life of this complaint, when Mr and Mrs S had essentially lost hope of repaying the loan and invested their hopes in this complaint. Although I haven't been able to consider the sale of the loan, I have found that there was more Together could have done to assist them.

Together should then calculate the amount of capital outstanding, disregarding any interest charged since 1 December 2020. It should work out what Mr and Mrs S will need to pay each month to clear the remaining capital balance between now and the end of the term. And it should then engage with Mr and Mrs S and review their income and expenditure to determine if that amount is affordable for them – and, if not, consider whether a term extension to reduce the monthly payment to an affordable amount would also be appropriate.

The responses to my provisional decision

Mr and Mrs S didn't agree with what I said about the time limits applicable to their complaint, as they said they were never made aware this was an unregulated loan, and weren't aware it was interest only. And they didn't know they could complain or how to go about complaining until recently. However, they welcomed my proposals for how to put matters right. They said paying the amount Together requested was simply unaffordable and has resulted in considerable distress.

Together said it had previously removed the 2016 and 2017 charges I had identified. It said removing the charges since 2022, and removing interest since December 2020, would reduce the balance from around £61,000 to around £47,000.

Together agreed to remove the arrears fees. But it didn't think freezing interest was a fair and reasonable outcome.

Together accepted that it could have done more to support Mr and Mrs S. But it didn't think it was fair that this should result in the loan being interest free from December 2020 onwards for the rest of the term. It said it was entitled to apply interest under the terms of the mortgage contract, and it wouldn't be right for Mr and Mrs S to benefit from any mistakes Together might have made.

It said that had it considered matters properly in December 2020, it might have offered to reduce the interest rate to zero for 12 months to allow Mr and Mrs S to take financial advice and explore "exiting" the loan if their circumstances are unlikely to change. To resolve this complaint, it offered to reduce the interest rate to zero from 1 December 2020 to 1 December 2023 to allow them to do that now. It said that would give them six months to find a way to exit the loan if they couldn't afford the repayments required. It said Mr and Mrs S would then need to pay £740 per month to clear the loan balance by the end of the term – subject to any future interest rate rises – though their contractual monthly payment was £510.

Together said that freezing interest on a permanent basis wasn't an appropriate form of assistance or a reasonable way forward. The purpose of an interest freeze is to provide temporary assistance – for the customer to either allow some time before resuming full payments, or allow some time to find a long term solution.

Mr and Mrs S then completed a further income and expenditure assessment. This showed that Mr and Mrs S's total income was around £2,850 per month, and their total expenditure was around £2,700 – this included the contractual monthly payment for this loan (but not the higher amount required to ensure it will be repaid by the end of the term). It said their expenditure included payments to non-priority unsecured debt, and that some of their other monthly expenditure was higher than might be expected. So it didn't agree that they couldn't afford to repay the contractual monthly payment plus an amount to reduce the balance.

Together said that following an interest freeze until December 2023, Mr and Mrs S would need to pay £740 per month to clear the loan balance by the end of the term – or £555 per month to clear the loan balance by April 2042 (a ten year term extension, the maximum it would consider), subject to interest rates changing over time. It considered this to be affordable according to the income and expenditure assessment.

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 also considered the responses to my provisional decision and the further arguments made.

I’ve noted what Mr and Mrs S have said. But I haven’t changed my mind about what I can consider as part of this complaint. I have no power to consider anything that happened before April 2014. And I’m satisfied that Mr and Mrs S would have been aware of fees they were being charged, and the amount outstanding, at the time. I can only consider things that have happened since 3 August 2015.

As I explained in my provisional decision, this is not and never has been an interest only loan. It was lent, and remains, on repayment terms. The reason Mr and Mrs S are in the position they are in now is because – due to past arrears and charges and associated additional interest – the payments they’ve been making barely cover the interest they’ve been charged each month, and so the balance is not reducing as was originally intended.

Together has refunded the fees I identified in 2016 and 2017, and has agreed to remove fees charged since 2022. It also agrees that it could have done more in 2020 to assist Mr and Mrs S. But it doesn’t agree that I what I said in my provisional decision is a fair way to put matters right – that’s the remaining point at issue in this case, and that’s what I’ll focus on.

It's unfortunate Mr and Mrs S haven’t made any payments since they made this complaint. I understand their position and that they felt there was no prospect of them ever paying off this loan. But not making any payments at all has left them in a worse position and withholding payment is never the right way forward – Mr and Mrs S should always pay what they can.

However, the key issue for me in this case is what happened before that, and whether Together treated them fairly in the run up to this complaint, and what it ought to have done to assist Mr and Mrs S in their particular situation.

As I said in my provisional decision, Mr S is disabled and unable to work. Mrs S is the sole earner (though they receive some benefits too) and she herself has health issues. Having considered the income and expenditure information they’ve provided, I think it’s clear that paying £740 per month to clear the loan by the end of the term wouldn’t be affordable for them. Although Together makes a reasonable point, with which I agree, that they could reach an arrangement – and should seek debt advice – in relation to their unsecured debt, I don’t agree that their other expenditure appears unduly high. And in some areas, such as utilities, it appears low in the current climate.

The interest rate was 8.7% initially. It increased to 10.7% in April 2008 and then remained unchanged until July 2020, when it reduced to 10.2%. Between June 2022 and now, it has increased to 13.7%. There is no guarantee that the interest rate won’t increase further between now and the end of the term – and if it does, and Together continues to apply interest, the amount Mr and Mrs S will be required to pay to clear the loan will increase further and become more unaffordable.

Together has proposed a term extension of ten years, which would reduce the required amount to around £555 (without any future interest rate rises) – which is more affordable for Mr and Mrs S. However, I’m not persuaded this would make the loan sustainable over the long term. As things are, the loan term will end when Mrs S is 65 and Mr S is 70. A ten year term extension would take them to 75 and 80, respectively. And it’s not clear the loan would be affordable for them past their retirement ages. So I’m not persuaded this is enough to put the loan on a sustainable footing.

I think it’s fair and reasonable to note that Mr and Mrs S have experienced substantial financial difficulties in the past – and that the impact of this has been to add significant extra interest to the loan balance. The result of this is that there's no clear sustainable way forward to ensure that the loan is repaid by the end of the term or in a reasonable time thereafter. If Mr and Mrs S resume paying what was affordable for them – around £500 per month – over the same loan term their position will continue to worsen and the shortfall balance at the end of the term will be larger than it is now. And extending the term would go significantly past retirement age, with no clear way for Mr and Mrs S to afford the loan at that point.

If Together had considered their situation in the round in late 2020, I think it would – acting fairly – have concluded that as things stood there was little or no prospect of Mr and Mrs S ever being able to repay this loan. And, rather than simply expecting them to "exit" the loan (which means, in reality, sell their property and move into rented accommodation – which also might not be affordable for them), it should, acting fairly, have considered whether there were any further forms of forbearance it could have shown to return the loan to a sustainable position.

In cases like this, reducing the interest rate, or freezing it altogether, is not uncommon in the second charge market, in my experience. For example, I note this is something the regulator referred to in its guidance to lenders in 2021.[1] Although this guidance post-dates the period when I consider Together could have done more in this case, and so is not something Together could have taken into account at the time, the measures set out in it represent existing good practice in approaching forbearance under the mortgage regulations.

In my view, this is a case where that would have been appropriate. It was clear that Mr and Mrs S had no prospect of repaying the loan by the end of the term. Paying what they could afford would either result in an increasing shortfall balance at the end of the term, or – as Together now offers but didn't at the time – a term extension significantly beyond their retirement ages. Reducing the amount due to what they could afford – by reducing the interest rate – would offer appropriate forbearance to deal with the issue of the escalating balance and ensure the loan could be repaid on time.

I take Together's point that in continuing to apply interest it would be operating the loan in accordance with the terms and conditions. The terms and conditions entitle it to charge interest as long as the loan remains outstanding. And that's a relevant factor. But it's also relevant to take into account whether strict enforcement of the contract without considering whether to vary it results in fair treatment in the particular circumstances of this complaint, taking into account also the wider obligations of forbearance.

For the reasons I've given, I'm satisfied that in the particular circumstances of this complaint, the fair outcome would be to restructure Mr and Mrs S's loan so that they're able to clear the balance in an affordable way over the remaining term – taking into account that past financial difficulty has resulted in an escalating balance which they otherwise wouldn't be able to pay off.

My final decision

For the reasons I've given, my final decision is that I uphold this complaint and direct Blemain Finance Limited trading as Together to:

- Remove all arrears fees charged since 2022, together with any interest charged on them.

- Reduce the interest rate to zero, backdated to 1 December 2020 and for the remainder of the loan term, and re-calculate the loan balance and monthly payment

[1] *Mortgages and Coronavirus: Tailored Support Guidance*, FCA, 2021 at para 5.18

accordingly.

- Write to Mr and Mrs S to confirm the revised loan balance and monthly payment.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr S and Mrs S to accept or reject my decision before 4 August 2023.

Simon Pugh
Ombudsman