DRN-4279724

The complaint

Mrs M has a mortgage with Kensington Mortgage Company Limited. She complains that Kensington wouldn't offer her a fixed interest rate product, change her interest-only mortgage onto a repayment basis, or offer her any meaningful support with her increasing mortgage interest payments.

What happened

Mrs M took out her mortgage with GE Money Home Lending Limited in 2007. She borrowed £87,750 over a term of 25 years, on an interest-only basis.

The interest rate on the mortgage was fixed at 6.34% for the first three years. It then reverted to a variable rate of 2.19% above the Barclays Bank plc base rate. In 2016, GE Money sold the mortgage to Kensington.

In April 2022, Mrs M got in touch with Kensington and asked whether she could switch to a repayment mortgage or take a fixed interest rate. Kensington said Mrs M's mortgage had a small arrears balance which she would need to repay before it could look into making changes to her mortgage. At the end of May 2022, Mrs M cleared the arrears.

In early June 2022, Mrs M contacted Kensington again to discuss her options. Kensington said it would send her an application pack to fill in to change the mortgage to a capital and interest repayment basis. Mrs M didn't receive the pack for several weeks. At the end of July 2022, she contacted Kensington to ask about the information she needed to include. Kensington received her completed application at the beginning of August 2022.

Mrs M says she waited for Kensington to get back to her and chased a response, and in October when she had still heard nothing, she complained about the lack of progress. She also set out her concerns about rising interest rates and asked again for a fixed rate.

Kensington said there had been some confusion following Mrs M's initial request to make changes to her mortgage, because it thought Mrs M hadn't been very clear about what she wanted. It nevertheless accepted it had caused some delay and provided poor service, so it paid Mrs M £500 for distress and inconvenience.

Kensington also said it couldn't offer Mrs M a new interest rate product, initially because it did "*not have the functionality*", and later because her mortgage originated with GE Money. It suggested she take independent advice. It later went through Mrs M's income and expenditure and offered to accept reduced payments for three months. But it said it couldn't change the mortgage to a repayment basis because this would result in Mrs M's monthly payments almost doubling, and she wouldn't be able to afford them.

Mrs M referred her complaint to the Financial Ombudsman Service, and said she was becoming increasingly concerned about her situation and the impact of rising interest rates. Our Investigator found that changing the mortgage to a repayment basis wouldn't be affordable for Mrs M, and that Kensington had been reasonable in offering a temporary payment arrangement to support her.

The Investigator also said that Kensington should have allowed Mrs M to take a fixed interest rate product when she asked for one in October 2022, given her concerns at that time about rising interest rates. He recommended that Kensington provide Mrs M with details of the products it had available at that time, allow her to choose one, and re-work her mortgage on that basis. He also recommended that it pay Mrs M an additional £250 compensation.

Kensington didn't accept that conclusion. It said that the fixed rates it has had available since October 2022 have consistently been higher than the rate Mrs M (who is on a rate which is tied to a base rate) has been paying – so she has saved money by not switching to a fixed rate. It also said that allowing her to take one of those rates now would give her the benefit of hindsight and would be unfair.

Our Investigator said Mrs M may choose not to switch to a different product, but he still thought she should have been given the option to do so.

Mrs M said she just wanted an affordable mortgage on a repayment basis over an extended term which she can afford, so that she doesn't have to worry about what will happen at term end.

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.

There's no obligation on lenders to offer new interest rates to their customers. A lender might legitimately choose not to offer rates to any customers. And where it does offer rates, it's fair and reasonable – and standard practice in the mortgage industry – for a lender to have eligibility criteria. These criteria might mean that not all borrowers are offered the same rate, or that some are not offered a rate at all, based on matters such as loan to value and arrears history.

In this case, Kensington has given Mrs M and our Investigator different reasons for refusing Mrs M a new rate, and its reasons have changed over time:

- It told Mrs M that she couldn't have a rate because it didn't have the functionality.
- It told Mrs M and us that she couldn't have a rate because her mortgage had originally been taken out with GE Money.
- It told us that the reason Mrs M couldn't have a rate was *not* because her mortgage had been securitised (i.e. because it was taken out with GE Money before 2010 and had since been securitised).
- It told Mrs M and us that she couldn't have a rate because all the products it had available had higher rates than the one she was currently on.
- It told us Mrs M couldn't have a rate because one of its criteria for a new rate is that the "*Reversion Margin on the new product is less than or equal to the Reversion Margin of the customers* [sic] *original product (i.e. from origination)*", and her mortgage didn't fulfil this requirement.

Kensington initially refused Mrs M a new rate because her mortgage originated with GE Money. This is because, as part of its business model, Kensington securitises its mortgages. This means it offers the beneficial interest in groups of loans to third party investors to raise funds for its ongoing mortgage business. This is a normal and legitimate feature of the mortgage industry, and it's not inherently unfair that Kensington operates its business in this way.

However, the Financial Ombudsman Service has in other cases taken the view that it's unfair for borrowers to be refused a new rate because of this, where the borrower can't move their mortgage to another lender or shop around for a better rate. I think Mrs M is likely to be in that position: she has an interest-only mortgage, and she has told us that she has looked for another lender, and she has had multiple discussions recently with an independent mortgage adviser – but her income isn't high enough for another lender to lend to her.

So if Kensington were to say that Mrs M must remain on her current mortgage deal, because of the way it has chosen to securitise her mortgage, and that in turn was based on when and how she took her mortgage out around 15 years before she asked about a rate in 2022, I would, in all the circumstances, consider this not to be a fair and reasonable basis on which to refuse her a new interest rate. Refusing Mrs M a new rate on this basis wouldn't be because of current characteristics of her or her mortgage – such as loan to value or arrears, or her wider credit risk.

The rules of mortgage regulation, to be found in the Financial Conduct Authority (FCA) Handbook under the heading MCOB, are relevant here. In particular, MCOB 11.8.1 E (the E means it's an evidential provision, not a rule) says that where a borrower is unable to move their mortgage to a new lender (as Mrs M was), their existing lender:

"*should not (for example, by offering less favourable interest rates or other terms) take advantage of the customer's situation or treat the customer any less favourably than it would treat other customers with similar characteristics. To do so may be relied on as tending to show contravention of Principle 6 (Customer's interests).*"

Principle 6 is another part of the FCA Handbook, and says that a firm:

"*must pay due regard to the interests of its customers and treat them fairly*"

Securitisation is not an unusual business model and not inherently unfair. However, this is not something Mrs M was aware of or had any control over. And I don't think it can be said to amount to a characteristic of Mrs M or her mortgage – it's something done to her mortgage by Kensington.

I don't therefore think that Kensington's choice to manage its business in this way is a relevant consideration for the purposes of the comparison envisaged by MCOB 11.8.1 E. It's a matter for Kensington's commercial judgement how it chooses to structure its business. But if – as I think is the case here – that results in unfairness in an individual case, that's a matter for me.

In my view, what's relevant is whether, when she asked for a new rate, Mrs M had similar characteristics to other borrowers who would be eligible for a new interest rate – and whether, if she did, refusing her a rate would tend to show unfairness of the sort envisaged by MCOB 11.8.1 E.

Kensington has provided details of its eligibility criteria, and said that Mrs M didn't meet one of them – that is: "*Reversion Margin on the new product is less than or equal to the Reversion Margin of the customers* [sic] *original product (i.e. from origination)*".

The information Kensington has given us about its available rates shows that Mrs M didn't meet this requirement in October 2022. This, however, will vary over time and is dependent on Kensington's changing offering – and I think it's hard to see its relevance. Mrs M might be prepared to take the risk of a higher reversion rate in future in return for the certainty of a fixed rate now. She might also, of course, subject to eligibility and availability, choose to take another new fixed rate in future before a reversionary rate on a new product takes effect. So I don’t think that the fact Mrs M’s mortgage didn’t meet this criterion at the time she asked for a new rate was a fair and reasonable reason to refuse her, bearing in mind her particular circumstances – which included that she had been on a variable reversion rate for a number of years and was very concerned about that rate increasing.

Kensington has also said it refused Mrs M a rate when she asked because the rate she was paying was lower than any of the fixed rates it had available, and also lower than its variable ‘Mortgage Prisoner’ rate. I think this is a valid consideration – although it is one for Mrs M rather than for Kensington. This isn’t one of the eligibility criteria Kensington has provided details of, and I share our Investigator’s view that it was for Mrs M to decide whether she wanted to pay a higher rate in return for the certainty of a fixed rate.

That said, the lowest fixed rate Kensington had available between October 2022 and May 2023 was a two-year fixed rate at 6.65% - which is higher than the rate Mrs M has been paying throughout that period. So Mrs M would need to think very carefully before taking that or another fixed rate, and if she does now choose one of the rates Kensington had available, resulting in her mortgage being reworked and backdated, she will need to make arrangements to pay Kensington the resulting shortfall – by way of a lump sum, additional payments agreed with Kensington, or by capitalising the shortfall. Mrs M should bear in mind that capitalisation would result in the mortgage balance, and in turn the monthly mortgage payments, increasing. I don’t consider that Kensington should fairly make good the shortfall, in the circumstances and given the uncertainty about whether a fixed rate would be cheaper in the long term.

Taking a new rate may cost Mrs M more in the long run – it’s impossible to say for sure, since that depends on how interest rates move in future generally, and what Barclays base rate, to which Mrs M’s current reversionary rate is tied, does in future specifically.

Choosing a new rate now to be implemented retrospectively does, as Kensington has pointed out, give Mrs M the benefit of hindsight when making her decision. That, though, is down to Kensington’s refusal to make its fixed rate products available to her earlier. Had it treated her fairly, she would have been able to decide whether or not to take a rate at the time of asking. I nevertheless understand Kensington’s point, and I agree it may not be fair in some cases to require it to backdate a rate.

In this case, though, Mrs M has been clear and consistent about her concerns about rising interest rates, and that is why she asked Kensington for a rate in October 2022. I agree with our Investigator that October 2022 is a fair starting point to take given Mrs M’s clear concerns about rate rises when she asked for a rate at that point, and given that she would be very unlikely to have taken a fixed rate in April 2022, when she initially approached Kensington about making wider changes to her mortgage. Kensington’s fixed rates were then also considerably higher than the variable rate Mrs M was paying.

In all the circumstances, I think Mrs M may well have chosen to take a fixed rate in October 2022, in order to protect herself against further rises on a variable rate. But even if she wouldn’t have chosen to do so based on the rates Kensington had available at that time, she should still have been given the option of doing so. I therefore find that she should fairly have the opportunity to take one of those rates now if she wishes to do so, with independent advice if necessary.

For these reasons, I don’t find that Mrs M should fairly have been refused a fixed rate for the various reasons Kensington has given. In all the circumstances, therefore, I’m satisfied that in refusing Mrs M a new rate, Kensington didn’t act fairly and reasonably.

Mrs M also asked Kensington about changing her mortgage onto a capital and interest repayment basis. Kensington's records show that it looked into this and considered Mrs M's income and expenditure to assess whether she could afford the resulting higher repayments. Her payments would have roughly doubled, and I think it's clear that this would have been unaffordable, as Kensington explained to Mrs M. So I don't consider Kensington treated Mrs M unfairly in not changing the payment basis of her mortgage. I also don't consider it was unfair in offering to accept reduced payments for three months when Mrs M asked it about what forbearance options it could offer her as she was concerned about her rising monthly payments.

Mrs M has told our Investigator that she wants to look into extending her mortgage term; doing this may make a switch to a repayment basis affordable. Kensington has said Mrs M hasn't yet asked it about this but it will consider a term extension if she asks. I leave it to Mrs M and Kensington to discuss this in the first instance.

Finally, I recognise that this matter has caused Mrs M considerable stress and anxiety. Mrs M has explained that it has affected her health and resulted in her needing to take time off work. I agree with our Investigator that £250 compensation in addition to the £500 Kensington has already paid is a fair and reasonable award in recognition of the impact its treatment of her, including its delays in dealing with her requests, has had.

Putting things right

In order to put things right, Kensington should give Mrs M the option of putting her in the position she would have been in had it offered her a rate when she asked in October 2022. Allowing time for an application to proceed, if Mrs M accepts this option, it should rework her mortgage as if a rate had been in place from 1 December 2022.

Kensington should provide Mrs M with a list of the rates it had available in October 2022. If Mrs M chooses to accept one of those rates, Kensington must re-calculate her mortgage on that basis – it will also be entitled to ask Mrs M to pay any shortfall because the interest rate she has been paying has been lower than the fixed rate. That can be by way of a one-off payment, additional payments over a period of time to be agreed between Mrs M and Kensington, or capitalisation.

Kensington should give any future application for a new rate fair consideration according to its criteria at the time, taking into account MCOB 11.8.1 E if it is still relevant at that time.

Kensington should also pay Mrs M £250 compensation.

My final decision

For the reasons I've given, my final decision is that I uphold this complaint and direct Kensington Mortgage Company Limited to:

- provide Mrs M with a list of the rates it had available in October 2022;

- if Mrs M chooses to accept one of those rates, Kensington should re-work her mortgage on that basis, backdated to 1 December 2022. This will result in a shortfall, which Kensington is entitled to ask Mrs M to pay by way of a one-off payment, additional payments over a period of time to be agreed between Mrs M and Kensington, or capitalisation; and

- pay Mrs M £250 compensation within 28 days of the date we notify it Mrs M has accepted this decision, if she does. If payment is not made within 28 days, simple annual interest of 8%* running from the date of notification to the date of payment should be added.

* If there is an 8% interest element to any payment to Mrs M, Kensington may deduct income tax from the 8% interest element as required by HMRC. But it should tell Mrs M what it has deducted so she can reclaim the tax from HMRC if she's entitled to do so.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs M to accept or reject my decision before 18 October 2023.

Janet Millington
Ombudsman