

The complaint

Mr W complains that in September 2023 The Mortgage Works (UK) (TMW) didn't immediately reduce his monthly direct debit payment when he made a significant lump sum payment to reduce his outstanding mortgage balance. He says it's unfair that TMW wasn't able to recalculate his monthly payments until the following month and wants a reimbursement of the additional interest he said he's paid.

What happened

In 2012 Mr W took out an interest only buy to let mortgage with TMW. His existing fixed rate mortgage deal expired on 31 August 2023 – after which Mr W said he wanted to stay on the provider's standard variable rate (SVR). In July 2023 Mr W made an overpayment of around 10% of his outstanding mortgage balance which meant he had little scope for further overpayment without incurring a penalty. So the day after the fixed rate expired Mr W made an overpayment of £85,000 to reduce his outstanding mortgage. Mr W says he assumed his monthly direct debit would reduce with immediate effect but when the payment left his account it was for over £1,000 which was equivalent to paying the SVR on the full outstanding balance – before the overpayment.

So he asked TMW to explain why the direct debit hadn't been reduced. It confirmed that there wasn't sufficient time for it to make a change after the overpayment was made – but in any case its usual process – as outlined in the mortgage terms and conditions (Ts&Cs) – was to amend a direct debit the month after any overpayment is made.

Mr W complained as he thought this was unfair, but TMW didn't uphold the complaint. It said the September direct debit was calculated based on the balance on 1 September 2023, before the overpayment was made. It said it had calculated the September payment correctly but would use the overpayment to recalculate the October direct debit.

I understand that later in September 2023 Mr W paid off the remaining balance of his mortgage.

Mr W wasn't happy with TMW's response, so he brought his complaint to us where one of our investigators looked into the matter. He didn't think the complaint should be upheld making the following points in support of his assessment.

- Mr W's mortgage offer stated that any overpayment would reduce the outstanding capital immediately but the amount of monthly interest payable wouldn't be amended until the following month.
- This was explained further in section 4 of the Ts&Cs. And TMW's website explained how overpayments worked with an actual example of how interest was applied.
- So he thought TMW had acted fairly and in line with the Ts&Cs and mortgage contract.

Mr W said he accepted that TMW had acted in line with its own Ts&Cs but thought that a common sense interpretation of them would suggest they were unfair and unreasonable. He also believed TMW hadn't abided by the new consumer duty regulations because this led to a poor consumer outcome for him.

The investigator said he had considered the question of the new consumer duty but didn't think it applied here because Mr W's mortgage agreement was in place before 31 July 2023 and TMW was entitled to rely on the terms set out in that agreement. He also explained that TMW's application of any overpayment was set out within Mr W's mortgage offer and its Ts&Cs, and he thought it had been applied in line with that here. He thought it had treated Mr W fairly and its method of applying the overpayment wasn't unusual in the market.

Mr W didn't agree. He said the clause in his contract was unclear and unfair. He said he didn't imagine it wouldn't be possible to *"pay off part of the capital in the first month of the mortgage that elapses from a fixed term onto a standard variable rate, in a way that decreases the interest payable on that capital sum paid."*

He said he would like his complaint to be referred to an ombudsman – so it has been passed to me to review.

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.

And having done so I agree with the outcome reached by the investigator. I know this outcome will disappoint Mr W – so I'll explain my reasons.

Mr W says he understands TMW's position here as set out in its Ts&Cs. But he doesn't think it's fair or customer focused. He says he couldn't have made an overpayment the day before he did because he would have suffered an early redemption penalty – so he was only able to make the payment on 1 September 2023 at the earliest. He says other lenders automatically adjust the outstanding interest payment straight away even if they have to adjust the following months direct debits if it's not possible to do so before the payment is due.

Mr W had a buy to let mortgage which is an unregulated product as defined by the regulator. So in this instance it's not something that's covered under the new consumer duty regulations. And calculating the interest on a monthly basis is the usual basis on which TMW operates – so I can't reasonably say it's acted unfairly as long as it's been clear about that fact. So I've looked at the relevant documentation – namely the buy to let mortgage Ts&Cs and Mr W's mortgage contracts.

The standard buy to let mortgage conditions first confirmed that Mr W must *"make monthly payments on the payment date each month during the repayment period until you have repaid the debt."*

Thereafter the interest that is repayable is charged on the capital balance *"at the end of each day"* and to work out the capital balance (section 4.2 b) *"any interest which remains unpaid at the end of the month in which it accrues will be added to the capital balance on the first day of the following month"*.

And section 4.2 d confirms the position with an overpayment with regards to the interest owed stating, *"any payment which is made to the credit of your account in any month (including a monthly payment, large overpayment or small overpayment) will reduce the capital balance on the first day of the following month."*

So, I think that's clear in setting out that TMW, as a standard with regards to buy to let mortgages, calculates the interest owed on the loan from the beginning of the following month – even if an overpayment to reduce the capital is made during a month.

And Mr W's original 2012 and subsequent mortgage contract – which was issued as a result of the product switch - has the following statements and clauses.

“11. What happens if you want to make overpayments?

If you make an overpayment the amount you owe us will be reduced immediately and the amount of interest you pay will be reduced from the first day of the following month.”

I think this further supports the idea that TMW operated a system of monthly interest calculation and also that, in my view, it made this very clear to Mr W in its literature and documentation.

In its response to Mr W's complaint, TMW suggested that there was insufficient time to change the direct debit payment as it was due the day after Mr W made his overpayment. But it would have been possible for TMW to work out the “run on” payment here and make any adjustment that was required the following month if it allowed for an alteration of the monthly payment due with immediate effect. So that wasn't the reason that TMW couldn't accommodate Mr W's request.

But TMW has subsequently confirmed to us that, *“our mortgage accounts are daily interest, monthly rest. Monthly rest refers to each month end when the outstanding balance is updated, and a new monthly payment is calculated if appropriate, taking into account any fees/charges debited to the account, or overpayments credited to the account during the month. The accounts are not daily interest, daily rest, because if that were the case then a payment calculation would've been triggered overnight on 1 September 2023, and a new reduced payment set with effect from 2 September 2023, but that's not how our accounts work.”*

I think that clarifies TMW'S position and, as it's in line with the information Mr W was provided with, I think it acted fairly and in line with how it said it would. I know Mr W believes that's unfair and isn't how other lenders for example would work, but TMW has shown clearly how it calculates outstanding interest due and, as long as it has made Mr W aware of that fact – which I think it has done – it's entitled to exercise that commercial decision which is the same for all its buy to let borrowers.

My final decision

For the reasons that I've given I don't uphold Mr W's complaint.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr W to accept or reject my decision before 22 May 2024.

Keith Lawrence

Ombudsman