DRN-4586558

Financial Ombudsman Service

The complaint

Mr and Mrs M have complained about the advice they were given by Believe Group Limited trading as Lendle Mortgages when taking out a secured (second charge) loan in 2019.

They've said:

- They were told they would be paying off capital and interest from the start, when in fact they were almost only paying interest, and still are.
- They've paid £23,000 to the loan over five years, but they've only paid £100 off the loan balance.
- They asked if it was like an unsecured loan they held which was front loaded with interest, and were told the interest wasn't front loaded and capital would be paid from the start.

What happened

Mr and Mrs M spoke to Lendle as they wanted to consolidate some of their debts, and Lendle gave advice about a second charge secured loan.

A secured loan offer was issued in February 2019 and that set out that Mr and Mrs M were borrowing £33,606 (including £3,596 that was borrowed to pay the set-up fees) over a 15-year term on a capital repayment basis. The interest rate was fixed at 12.50% for the first five years, after which it would move to the lender's standard variable rate (which was 12% at the time of the offer). That gave an initial payment of £414 a month. The offer said that if nothing changed, and the loan ran for the full term, Mr and Mrs M would pay back £73,749.

In June 2023 Mr and Mrs M raised a complaint. Lendle issued its final response letter in July 2023 in which it didn't uphold the complaint. Unhappy with that Mr and Mrs M referred their complaint to our service.

Our Investigator said the interest wasn't front loaded, it was a standard capital repayment mortgage (secured loan) upon which the balance will always reduce more slowly at the start. She said the addition of fees meant the opening balance was higher and Mr and Mrs M's outgoings were significantly lower with this loan as it was to be paid off over 15 years.

Mr and Mrs M said they wanted the complaint to be passed to an Ombudsman to decide. They said the main point of their complaint is that it clearly states in the transcripts of their conversations with Lendle that they asked if the interest was front loaded like a loan they were paying off, and they were assured it was not the same product.

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.

Although I've read and considered the whole file I'll keep my comments to what I think is relevant. If I don't comment on any specific point it's not because I've not considered it but because I don't think I need to comment on it in order to reach the right outcome.

I think at the crux of this complaint is a misunderstanding about how Mr and Mrs M's loan interest was calculated. To try to help I will first explain, in more general terms, about how loan interest can be calculated. I will then talk about Mr and Mrs M's specific loan.

There are two ways the interest can be calculated on loans:

Option one – which is how Mr and Mrs M's secured loan works

This is a monthly interest loan so when the customer makes a payment their interest is calculated for the following month based on that new lower balance; that's the monthly interest element. That can be seen from Mr and Mrs M's loan terms and conditions which say:

> *"Interest is calculated and charged to your mortgage account at the Rate of Interest each month on the date when the Monthly Payment is due."*

The easiest way to think about this is using an example of a customer with a loan of £33,600 and a contractual monthly payment of £414 (all figures are rounded and approximate, and just for illustrative purposes):

- An opening balance of £33,600.
- Month one they pay £414. £350 of that payment goes to cover the interest, which leaves £64 to go to repay the debt. So the loan balance is now £33,536.
- Month two the payment stays the same, so they still pay £414. As the balance is lower, £349 goes to cover the interest, leaving £65 to reduce the debt. The balance is now £33,471.

That would then continue throughout the life of the loan, with the interest added each month based on what the balance is on the date the monthly payment is due. This is how Mr and Mrs M's loan works.

Based on the original loan agreement, if Mr and Mrs M's loan runs for its full 15-year term, they make all their payments in full and on time and the interest rate doesn't change they will pay £73,749 in loan payments (including interest).

Option two – which was not how this loan is calculated

Some lenders added all the interest onto the loan upfront and it seems this was the case with the loan Mr and Mrs M were replacing which they asked Lendle about.

Using the same figures as an example (so a customer borrowing £33,600 with a contractual monthly payment of £414), instead the lender would have used an opening balance of £73,749 (that is, the total amount the lender expected the customer to pay over the life of the loan).

A loan where all the interest is added on day one would, instead of the above, look like the following:

- An opening balance of £73,749 (rather than £33,600).

- Month one the full £414 comes off the balance, so the loan balance is now £73,335.
- Month two the payment stays the same, so they still pay £414. The full £414 again comes off the balance, so the loan balance is now £72,921.

The first scenario is how a normal capital repayment mortgage or secured loan works (albeit sometimes the interest is worked out daily and other times monthly, here it was monthly).

The second scenario is what is known as front loading the interest. Front-loaded interest has a very specific meaning, and this secured loan does not have front-loaded interest.

This is a capital and interest repayment loan, so the capital would be paid off throughout the loan term, and it wasn't just the interest being paid at the start. In any form of lending the majority of the monthly payment at the start will be going towards interest, that's because the balance is at its highest point and interest is paid on that full balance. Conversely, by the end of the term the balance is almost paid off so the majority of the monthly payment goes towards paying the capital as there is only a small amount left for interest to be charged on. That is entirely normal, and Mr and Mrs M would be unable to find any form of fixed term borrowing (other than interest-free agreements) that wouldn't work this way. This is called loan amortisation.

Mr and Mrs M have said:

> *"To date from a £30k loan after just under 5 years we have paid around £25k into the loan and still owe £29,900 of the balance.*
>
> *We have only paid off the fees."*

But they haven't paid the fees off, the fees just form part of the total overall borrowing as Mr and Mrs M opted to add them to the loan debt and the fees will be repaid, plus interest, over the full 15-year term. And so Mr and Mrs M didn't have a £30,000 loan, they had a £33,606 loan. Mr and Mrs M took out a £33,606 loan and they said the balance was £29,900. That means, at the point in time they're referring to, they'd paid around £3,700 off the capital of their debt.

Mr and Mrs M have also said that if they'd kept their unsecured debts there would only be around five years left and they would have saved around £20,000. But they also would have been paying out around £800 extra each month (across all their debts which were consolidated into this loan).

If Mr and Mrs M had opted for a shorter term on this loan such that their payments were £800 higher a month, then that also would mean they'd have had a much shorter term and would have paid less interest. For instance, if Mr and Mrs M had opted for a ten-year term on this loan then they would have needed to pay around £490 a month, and they'd have paid around £15,500 less interest over the life of the loan. And if they'd opted for a five-year term on this loan then they would have needed to pay around £750 a month, and they'd have paid around £29,200 less interest over the life of the loan.

Having considered everything very carefully I don't find that the adviser misled Mr and Mrs M as to how their loan would work in respect of the payment of interest and capital, and I'm satisfied the loan Mr and Mrs M have is as it was described by the adviser and as was set out in the illustration.

My final decision

I don’t uphold this complaint.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr and Mrs M to accept or reject my decision before 15 April 2024.

Julia Meadows
Ombudsman