

The complaint

Mr S and Mrs S complain about the way Barclays Bank UK PLC have applied an Early Repayment Charge (ERC) to their mortgage.

What happened

The interest rate product on Mr S and Mrs S's Barclays mortgage was due to expire in May 2023. In September 2022, as a result of the rise in interest rates and the uncertain economic climate, Mr S and Mrs S applied, via a mortgage broker, to switch to a new interest rate product. They applied for a five year fixed rate of 3.23%, and wanted the new rate to start on 1 June 2023 upon the expiry of their existing rate. They were told by Barclays that the latest they could switch to that rate would be 29 March 2023, as completion had to take place within 180 days of the application. Barclays also told Mr S and Mrs S that in order to complete the application, they would need to pay an ERC of 2% of the outstanding balance (£17,561.28) within 30 days in order to secure the rate. Mr S and Mrs S paid the ERC and the new rate was arranged.

In January 2023 Mr S and Mrs S complained to Barclays. They were unhappy that the ERC that Barclays charged was 2% of the balance as it was in October 2022, rather than 2% of the balance at the time the rate switch was due to take place in March 2023, as that was when the mortgage would be 'redeemed'. They also felt the ERC itself was unreasonable, excessive, and unfair and didn't comply with the guidelines set out in the Financial Conduct Authority's (FCA's) Mortgage Conduct of Business Sourcebook (MCOB) because:

- They've moved to a higher rate with Barclays, and are switching to that rate two months early, so Barclays should not be at a loss.
- The redemption is only two months before the end date and the cost to the bank of £17,500 when they've switched to a higher rate seems excessive.
- The expected lending rates in March 2023 will be much higher than the 1.97% Mr S and Mrs S were paying on their mortgage. So the money redeemed in March will be lent by Barclays at a much higher rate and they won't be at a loss.

Barclays issued their final response letter on 30 January 2023. They said when they offer a fixed rate, the money to facilitate the product has been borrowed from the open market, typically in the form of a bond. The rate they pay on a bond is determined by the interest rates at the time with the products they then offer to customers designed around the amount borrowed, along with the rate charged. So the rates available to Mr S and Mrs S in 2021 would have been based on the mortgage markets at that time as well as being competitive against other lenders. The ERC was a condition of the mortgage which is designed to compensate the bank for interest it will lose out on should Mr S and Mrs S repay the mortgage early. They wouldn't waive the ERC as it forms part of the mortgage contract. The details of the charge were in the offer.

Mr S and Mrs S brought their complaint to our service. They said they felt Barclays had not performed their Consumer Duty by not advising them to reduce their balance as much as they could before paying the ERC or switching the rate. Mr S and Mrs S said they were vulnerable at the time due to the shock of the sudden rate rises following the mini budget. They also felt it was unfair that a product fee of £999 was added to the mortgage on

application of the new rate, which then attracted interest before the new product had even started.

Our Investigator looked into things, and upheld the complaint. He said to put things right Barclays should:

- 1) Calculate the ERC based on the mortgage balance on the day Mr S and Mrs S's new rate took effect in March 2023.
- 2) Refund the difference between 1) and the ERC Mr S and Mrs S paid in October 2023.
- 3) Add 8% simple interest on the amount to be refunded. This should apply from March 2023 to the date of settlement of the complaint.
- 4) Refund the interest charged to the product fee of £999 between the date of the product fee being applied, and the date Mr S and Mrs S's new rate took effect in March 2023.
- 5) Pay Mr S and Mrs S £200 for the distress and inconvenience caused.

Barclays accepted the outcome but said the 8% simple interest would be calculated from the date the full ERC was charged, until when it should have been charged in March 2023. They would then calculate 8% on the excess ERC amount charged from March 2023 to the date of settlement. They didn't agree to refund the interest charged on the product fee as they said Mr S and Mrs S had the option of paying that fee upfront rather than adding it to the mortgage balance. The fee is payable at the time the rate is booked. They offered to increase the award for distress and inconvenience to £350.

Mr S and Mrs S didn't feel the redress went far enough to compensate them for what had happened. They said that if they'd been told in October 2022 that the ERC would be charged in March 2023 based on the balance at that time, they would have had the opportunity to make overpayments to the mortgage and reduce the balance. That way they could have reduced the amount of ERC payable, and the balance that the new higher interest rate would be charged on. So using the actual balance as it was in March 2023 to form the calculation was unfair. They also felt the award for the distress and inconvenience caused should be increased to £5,000. Mr S said he was diagnosed with an inflammatory disease in March 2023 and believes the distress caused by Barclays contributed to this.

Our Investigator considered what both parties said, and issued another opinion. He no longer felt that the interest on the product fee should be refunded, as the fee was payable at the time of application to book the rate, and Mr S and Mrs S had the option to pay the fee upfront or add it onto the mortgage. He also agreed with the way Barclays had proposed to pay Mr S and Mrs S the 8% simple interest on the ERC amount that Mr S and Mrs S overpaid in October 2022. He thought the increased distress and inconvenience award of £350 was reasonable. The rest of his outcome was unchanged.

Mr S and Mrs S asked for the complaint to be passed to an Ombudsman. They said they had the means and ability to make overpayments of £300,000 to £500,000 between October 2022 and March 2023. If they'd known in October 2022 they didn't have to pay the ERC until March 2023 they would have had the opportunity to make those overpayments and reduce the balance and therefore the ERC. If Barclays had not made them pay the ERC in October 2022, they would have had the headroom to think about overpayments, and the reason they didn't make any during that period was because they were reviewing the relevant FCA guidelines and engaged financial advisers and solicitors before sending their complaint letter in January 2023. After the final response was issued, they were occupied drafting the complaint to our service. Around the same time Mr S became unwell as a result of the stress caused. Within around two months of complaining to our service they had the headroom to review the mortgage balance, liquidate their assets in excess of £87,000 and pay off part of

the balance. They said they could have done this before March 2023 if it wasn't for Barclays' wrongdoing.

The Investigator wasn't persuaded to change his outcome and so the complaint has been passed to me to issue a decision.

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.

Barclays have accepted that they shouldn't have charged Mr S and Mrs S an ERC on their mortgage until the product switch took place in March 2023. So what remains for me to decide is how Barclays should put things right.

The ERC

Mr S and Mrs S's mortgage offer set out the ERC that would be charged if they redeemed their mortgage before 31 May 2023. The offer said the ERC would be 2% of the amount repaid. They repaid their mortgage to take out a new interest rate product in March 2023, so I'm satisfied an ERC was payable.

Mr S and Mrs S have said that if Barclays told them in October 2022 that the ERC would be charged in March 2023 on the balance as it would be at that point, they would have made overpayments of £300,000 to £500,000 to reduce the amount of ERC they would have to pay. They didn't make any overpayments during that period, but Mr S and Mrs S said that was because they were focusing on their complaint, and then in March Mr S was diagnosed with an inflammatory disease. I'm sorry to hear about what Mr S and Mrs S have been through during this period, and can appreciate this was a stressful time for them.

Whilst Mr S and Mrs S have said they had the means to make significant overpayments before the rate switch in March 2023, in order for me to decide that Barclays should factor in those hypothetical overpayments into the redress, I'd have to be satisfied on the balance of probabilities that had things happened as they should have done, those overpayments would have been made, and so the ERC payable in March 2023 would have been lower. Having carefully considered the information provided by both parties, I'm not persuaded they would have been.

I say that because firstly, the terms of Mr S and Mrs S's mortgage as it was at the time stated there was a limit on the amount of overpayments Mr S and Mrs S could make on their mortgage at 10% of the balance per year. So the maximum overpayment Mr S and Mrs S could have made without incurring an ERC was around £88,000. Nothing was preventing Mr S and Mrs S making an overpayment of that amount notwithstanding the information they were given about the ERC.

Whilst Mr S and Mrs S have said that had they been correctly informed, they would have had the motivation to make the overpayments to reduce the ERC, Mr S and Mrs S already had a motivation to make overpayments if they could, as they would have reduced the amount outstanding at the time the higher interest rate became payable, and therefore they would have paid less interest on the mortgage overall. I appreciate Mr S and Mrs S were focusing on their complaint during the relevant period, but I'm not satisfied this meant they were unable to make overpayments on their mortgage.

Mr S and Mrs S have also made reference to the 'Consumer Duty'. This is a new standard introduced by the FCA. It sets higher and clearer standards of consumer protection across financial services and requires businesses to put their customers' needs first. Mr S believes

that as Barclays did not encourage Mr S and Mrs S to reduce their mortgage balance before paying the ERC, they were failing in their Consumer Duty. The Consumer Duty applies to open products and services from 31 July 2023, and so it was not in effect at the time Mr S and Mrs S chose to switch their mortgage product and does not apply.

However, Barclays did still have a responsibility to treat Mr S and Mrs S fairly, and give them information that was clear, fair and not misleading. Barclays should have explained that the ERC would be payable at the time of the product switch in March 2023. But I'm not persuaded there was an obligation for them to go beyond that and advise Mr S and Mrs S to reduce their balance as much as possible before then. Barclays had not advised Mr S and Mrs S to make this product switch, that advice had been given by Mr S and Mrs S's broker. As such, it was the broker's responsibility to advise Mr S and Mrs S on the suitability of the new interest rate product, and the implications of them switching early, not Barclays'.

Overall, I'm not persuaded Barclays' actions prevented Mr S and Mrs S from making the overpayments they say they would have made, and so I don't think it would be reasonable for Barclays to factor them into the redress for this complaint.

As Barclays have said the ERC should have been charged on 29 March 2023 on the balance as it was at that point, I'm satisfied Barclays should refund the difference between the ERC Mr S and Mrs S paid, and what they should have paid had it been charged on the correct date, based on the balance as it was at that time. They should also pay 8% simple interest on the whole ERC amount Mr S and Mrs S paid between the date it was paid in October 2022, and the date it should have been payable on 29 March 2023. Barclays should then pay 8% simple interest on the difference between the two amounts calculated from the date the ERC should have been paid on 29 March 2023, to the date of settlement.

Mr S and Mrs S are also unhappy with the amount of ERC charged because the product switch only took place two months before the existing product was due to end, and because Mr S and Mrs S were switching to a higher interest rate than what Barclays were expecting to receive for those two months. As a result, they don't believe Barclays suffered a loss and therefore should not have charged an ERC.

Mr S and Mrs S have pointed to the rules set by the regulator. MCOB 12.3 sets out the requirements for lenders when setting their ERCs. In summary the rules say that the ERC must be expressed as a cash value, and that it must be a reasonable pre-estimate of the costs as a result of the customer repaying the mortgage early. The guidance also says the lender can choose the method it uses to calculate the ERC, and it can be calculated across a tranche of mortgages of a similar type, rather than on each individual mortgage for individual customers.

I'm satisfied the ERC was set out clearly in Mr S and Mrs S's mortgage offer. It was expressed as a cash value, and it was clear that the charge would be payable should the mortgage be repaid before 31 May 2023.

Barclays have sent our service information about how the ERC was calculated for the tranche of mortgages that included Mr S and Mrs S's mortgage product. That information shows that when calculating the ERC of 2%, Barclays took into account a number of factors when estimating the cost to them of the mortgage being repaid early. This included the variable costs they would likely incur to unwind the funding used to lend the mortgage, as well as the fixed costs they would incur on things such as advisers and underwriters. On review of that information, I'm satisfied Barclays set the ERC of Mr S and Mrs S's mortgage product at a level that was a reasonable pre-estimate of their costs upon early repayment.

Mr S and Mrs S have said that the ERC Barclays charged them was not reflective of the

actual costs incurred by Barclays, as the rate they were switching to was higher than what they would have paid if they'd continued on their existing rate, they cannot see how Barclays could have made a loss. I've explained there are costs incurred by Barclays for making changes to the mortgage within the term, regardless of the fact that Mr S and Mrs S were switching to a higher rate of interest. It's not as simple as Barclays just receiving more money than they would otherwise have done had Mr S and Mrs S not switched.

I appreciate that Mr S and Mrs S switched their product only two months before it was due to end, and so the amount of the ERC appears out of proportion to the number of payments that were remaining under the fixed rate. But that isn't a factor in how the ERC is calculated, nor is the actual cost to Barclays of this individual mortgage being repaid at the exact time it was. MCOB only requires Barclays to make a reasonable pre-estimate of the cost to it of the mortgage being repaid early across a range of similar mortgages. I'm satisfied that is what they've done.

The product fee

Mr S and Mrs S complain that the product fee Barclays charged in October 2022 to secure the new product was unfairly added to the mortgage balance in October, and so incurred interest before the new product had started.

It is common practice for the product fee to be charged upon the agreement of the new product being secured. In Mr S and Mrs S's case, they had requested for the start date of the new product to be pushed back as late as possible, but Barclays had still arranged and agreed to the new product in October. I'm satisfied it was fair for Barclays to charge Mr S and Mrs S for securing the new product at the time it was arranged in October 2022.

Barclays gave Mr S and Mrs S the option to pay the fee upfront, which would have avoided them having to pay interest on it. Mr S and Mrs S chose to add the fee to the mortgage. That was their choice to make.

As a result, I'm not persuaded Barclays acted unfairly when they added the product fee to the mortgage in October 2022.

Distress and inconvenience

If things had happened as they ought to have done, Barclays would have charged Mr S and Mrs S their ERC in March 2023 rather than October 2022. That is the mistake I'm satisfied has been made here. So when deciding on a reasonable award Barclays must pay for the distress and inconvenience caused to Mr S and Mrs S, I'm only able to consider the direct distress and inconvenience caused by that mistake.

Mr S and Mrs S should have had more time to arrange the funds to pay for the ERC than they did. I'm satisfied £350 is a fair reflection of the distress and inconvenience Mr S and Mrs S suffered because of that. I do appreciate Mr S had become unwell during this period too, and he and Mrs S have said they were worried about the wider economic climate and the impact this would have on them as well. This would undoubtedly have caused them additional stress at the time of trying to sort out their new interest rate product. But I'm not persuaded I can attribute all of that stress to Barclays' mistake. As a result, I'm not persuaded it would be reasonable to direct Barclays to increase the offer they've made.

Putting things right

For the reasons I've set out above, I'm satisfied Barclays should do the following to put things right for Mr S and Mrs S:

- Refund the difference between the ERC Mr S and Mrs S paid in October 2022 and the ERC they would have paid if it was calculated on their mortgage balance as it was on 29 March 2023.
- Pay Mr S and Mrs S 8% simple interest* on the above amount calculated from the date the ERC should have been paid on 29 March 2023, to the date of settlement.
- Pay Mr S and Mrs S 8% simple interest* on the ERC amount paid in October 2022 calculated from the date the ERC was paid, to the date it should have been paid on 29 March 2023.
- Pay Mr S and Mrs S £350 for the distress and inconvenience caused.

*Interest is at the rate of 8% a year simple. If Barclays considers that it's required by HM Revenue & Customs to take off income tax from that interest, it should tell Mr S and Mrs S how much it's taken off. It should also give them a certificate showing this if they ask for one, so they can reclaim the tax from HM Revenue & Customs if appropriate.

My final decision

Considering everything, for the reasons I've explained, I uphold this complaint and direct Barclays Bank UK PLC to put things right as I've set out above.

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 28 March 2024.

Kathryn Billings
Ombudsman