DRN-4618415

The complaint

Mr S complains about how Clydesdale Bank Plc, trading as Virgin Money, allocated the payments he made to his credit card account.

What happened

Mr S has a credit card account with Virgin Money. His credit card balance consists of an amount which incurs interest (I will call this his “purchase balance”), and also a number of interest-free “instalment plans”, in which the balance of each plan is repaid monthly over a certain number of months. (Each instalment plan also has a small monthly fee.)

According to the account’s terms, the minimum payment each month consists of charges, interest, 1% of the purchase balance, and 1% of the instalment plan balances and their associated monthly fees. If more than the minimum payment is paid into the account in any given month, then the additional payments are supposed to be allocated in a particular order: firstly to the rest of the monthly instalment plan payments; then to the remaining balances, in the order of highest interest rates to lowest (so the purchase balance and then the instalment plans); and finally to any new transactions which are not yet showing on a monthly statement. Because of the amount Mr S paid in each month, he expected most of his payments to be allocated to his purchase balance; this would reduce the amount of interest he would have to pay.

However, in March 2023 Mr S complained to Virgin Money that this order of allocations had not been followed. He said that in December 2022 and since then, his payments had been misallocated almost entirely to his instalment plans instead of to his purchase balance. The result was that his purchase balance had not been reduced, and so he had ended up paying more interest than he should have.

Virgin Money did not uphold Mr S’s complaint; it insisted that it had been allocating his payments correctly. (However it did pay him £80 for some customer service issues.) Being dissatisfied with that response, Mr S brought this complaint to our service.

One of our investigators found that three of Mr S’s zero-interest instalment plans had been paid off earlier than scheduled, instead of his payments being applied towards the purchase balance. That meant that the purchase balance had not been reduced as much as it should have been, increasing the amount of interest Mr S had been charged. As Virgin Money had been unable to explain this, the investigator upheld this complaint. He said that Virgin Money should adjust Mr S’s interest accordingly, so that he would not be out of pocket, and also pay him £300 for his trouble.

Virgin Money did not accept that opinion. It said that the payments had been correctly allocated in line with the account’s terms and conditions. It later provided a further explanation of this, after the investigator had issued his opinion. Virgin Money said that the allocations had not happened in the way which Mr S had expected, because one of his recent purchases had not yet appeared on a monthly statement, meaning that it fell into the category which is paid last in the order of allocations, instead of it falling in his purchase balance. That meant that the instalment plans had taken priority over it. Since the purchase balance in Mr S's next statement had consisted mostly of that new purchase, it had barely been reduced. That was not the result of any banking error.

The investigator remained unconvinced. As agreement could not be reached, this case was referred for an ombudsman's decision. I wrote a provisional decision which read as follows.

What I've provisionally 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.

On 5 December 2022, Mr S's statement was generated. It said that his total balance was £4,946:75. This consisted of a purchase balance of £1,493:65 (which was almost entirely made up of a single purchase which Mr S had made on 11 November), and five instalment plans with balances and fees adding up to £3,453:10.

That statement asked Mr S to make a "Requested Payment" of £580:16. This consisted of the minimum payment plus the five monthly payments which Mr S was required to make under the five instalment plans.

The next day, on 6 December 2022, Mr S spent £1,587:09 in one transaction. The post date was 7 December. Then on 9 December, Mr S created a new instalment plan for that amount. I will refer to the new plan as "plan 6."

At the end of paragraph 11 of the account's terms and conditions, it says:

> "We will always pay off existing balances that appear on your statement, before any from transactions that you have made but are not yet shown on a statement."

Therefore that £1,587:09 transaction and the balance of plan 6 were the lowest priority in the order of payment allocations made in December.

Between 9 and 29 December, Mr S made four payments into his account. These added up to £1,733:16 in total. The first payment, which he made on 9 December, was for the Requested Payment of £580:16. The next three payments add up to £1,153 precisely.

I have already summarised the order in which these payments were supposed to be allocated, but to help me better describe the allocations process, I will now give a number to each stage in that process, although no such numbers are given in the terms and conditions.

The minimum payment is allocated first, and I will call this step 1. This goes towards any charges and interest, 1% of the total account balance, and 1% of all the instalment plan fees. Steps 2 to 4 then apply to any payment above the minimum.

In step 2, payments are allocated to the remainder of the monthly instalment plan payments, in the order of when each plan is scheduled to expire, from the earliest end date to the last.

The Requested Payment on each statement consists of the total amount of money which (if paid) would be allocated under steps 1 and 2. As I've said, in December 2022 Mr S paid £1,153 more than that, which therefore fell to be allocated under steps 3 and 4.

Step 3 is allocation to the remaining balances on the statement, in the order of highest interest rates to lowest. In Mr S's case, this means the purchase balance first, and then the remainder of the original five instalment plan balances (in the same order as in step 2).

Step 4 is allocation to any balances from new transactions which are not yet showing up on a monthly statement. In December 2022, that included instalment plan 6 and the transaction which was posted on 7 December (which both represent the same sum of money, £1,587:09). In other words, plan 6 and the related purchase were not part of step 3.

The result was that all of the £1,153 was allocated to the balances that already existed on 5 December, and which had appeared on the statement of that date. There was no money left for step 4.

Those balances were an interest-bearing purchase balance – which on 5 December was £1,493:65 – and five interest-free instalment plan balances. So Mr S thought that all of the £1,153 would be allocated to reduce the purchase balance under step 3.

However, that didn't happen. It was all allocated to the five instalment plans instead.

It is not in dispute that that is what happened; rather, Virgin Money says this is actually what was supposed to happen. Virgin Money gave a very detailed explanation in an email it sent to our investigator. I will summarise that explanation here.

It all has to do with what happened when instalment plan 6 was created on 9 December. As I've said, plan 6 was for a transaction of £1,587:09 which Mr S had made three days earlier. Behind the scenes, that new purchase was not added to the existing purchase balance; it was recorded separately, in what I will refer to as "the unstatemented balance". The purchase balance didn't change. And then when plan 6 was created, Virgin Money's systems automatically deducted plan 6's balance from Mr S's purchase balance. That reduced the payment balance from £1,493:65 to zero. (Only the remainder, nearly £100, was deducted from the unstatemented balance, which became £1,493:65.)

That is not how Mr S expected it to work. He thought (not unreasonably) that the new transaction that he'd made on 6 December had just been added to his purchase balance, and that creating plan 6 would then deduct it again, returning his purchase balance back to what it had been on 5 December, £1,493:65. Then any payments which he would make later on would reduce that purchase balance, under steps 1, 2 and 3. But instead, unknown to him, Virgin Money was actually treating any new purchases (the ones which would fall within step 4) separately to the purchase balance until they appeared on his next statement, on 5 January.

In other words, new purchases don't get added to the purchase balance until they appear on the next monthly statement. Meanwhile, they are kept in the unstatemented balance instead.

The effect of all of this was that when Mr S's four payments were allocated under steps 1, 2 and 3, there was no purchase balance to allocate the payments to. So they all went to the original five instalment plans – apart from £2:21, which was used to pay off what little was left of a balance transfer (which had mostly been paid off in November).[1] Then in the next statement, dated 5 January, the unstatemented balance of £1,491:44 became the new purchase balance.

That meant that Mr S was not charged any interest in December. But it also meant that his new purchase balance in January was almost the same that it had been a month ago, instead of being reduced by 1% plus £1,153. So he was charged more interest in January than he would have been if things had gone the way that he expected.

[1] The unstatemented balance was reduced by this amount, for reasons which don't concern us here.

I accept that Virgin Money's explanation is true, because it adequately explains what happened and is consistent with the evidence. But I also need to decide whether how its system operates actually conforms to the account's terms and conditions.

As I've explained, there were two events that happened which, in combination with each other, led to an unexpected result. These were: (1) the new transaction on 6 December did not change the purchase balance; and (2) when that transaction was later moved to a new instalment plan, that reduced the purchase balance. Taken together, these two events meant that the purchase balance was reduced to zero.

However, it was not unexpected that creating plan 6 would reduce the purchase balance – Mr S had intended that to happen. I'm satisfied that event (2) happened in line with the terms and conditions. That this resulted in the unexpected reduction to zero was the result of event (1).

I have already quoted from the terms and conditions, but for the reader's ease of reference here is that clause again (this time with my emphasis added):

> "We will always pay off *existing balances* that appear on your statement, before *any from transactions* that you have made but are not yet shown on a statement."

I think that it is a reasonable interpretation of the phrase *"existing balances"* to say that it includes the purchase balance as it stood on 5 December, but excludes that balance being increased by any new transactions made after that date (until the next statement date). And *"any* [balances] *from transactions"* made since then means not only instalment plans created for new transactions, but also any other balance arising from new transactions which are not put into an instalment plan (or before they are put into a plan), such as any portion of a future purchase balance attributable to such a transaction. So both halves of that clause make it necessary for the bank to add new transactions to an unstatemented balance, rather than to the purchase balance. For that reason, I think that event (1) happened in accordance with the terms and conditions too.

I am therefore minded to conclude that Mr S's payments in December, and in the following months, were allocated correctly, and not as the result of a banking error.

Responses to my provisional decision

Mr S did not accept my findings. He raised the following points:

1. I had ignored the fact that the only transaction he had made in the statement period ending with 5 December 2022 (which was for £1,491:44) had been converted to an interest-free instalment plan in the same month, and yet it had still been included in the purchase balance on the 5 December statement. So the transaction appeared twice, in two different balances – the purchase balance and the instalment plan.

2. He questioned the £2.21 amount which had remained from an earlier balance transfer (mentioned above).

3. He asked for clarification about the relevance of plan 6, and the related transaction of £1,587:09.

4. I had not explained what Mr S could have done differently if he wanted to reduce his purchase balance to nil.

5. In step 3, payments were supposed to be allocated in the order of highest interest rates to lowest – meaning the purchase balance first, followed by the instalment plans – but this had clearly not occurred, because in January there was still a purchase balance of £1,491:44.

6. His complaint had not just been about the misallocation of payments. It had also been about inaccurate statements which showed the wrong purchase balances.

7. I had said in my provisional decision that the purchase balances in December and January were “almost the same”, but they were actually identical.

8. In the same paragraph, I had written that things had not gone the way he had expected, but in fact his expectations had been exactly what I had described in my description of step 3.

My findings

I will deal with each of Mr S’s points in the same order as set out above, each under its own heading, except that I will deal with points 3, 5 and 8 together because the answers are related.

<u>1: The transaction for £1,491:44 has been counted twice</u>

The transaction for £1,491:44 was made on 11 November 2022. The post date was 13 November. On 14 November, Mr S created an instalment plan for the same amount, and I will call this “plan 5”.

Exactly the same thing happened with plan 5 as happened with plan 6. The new transaction for £1,491:44 was not added to the purchase balance, but to the unstatemented balance instead. When plan 5 was created, the old purchase balance from the 6 November statement was reduced by £1,491:44. But plan 5 and the related purchase were not part of step 3 for that month. Then on the next statement date, 5 December, the unstatemented balance was added to the purchase balance, which became £1,493:65 (consisting of £1,491:44 and £2:21; I explain the latter amount below).

The reason I did not go into all of this in my provisional decision was only because I thought that explaining what had happened in one month (I chose December 2022) would be sufficient to illustrate how the system works. I didn’t ignore it, I just didn’t think it was necessary to explain November and January too.

<u>2: The £2:21 left over from November</u>

The £2:21 is interest which was charged on a balance transfer that had reached the end of its promotional rate.

In October 2022, Mr S had a balance transfer of £2,420:35 on a promotional interest rate of zero, which was due to come to an end on 5 October. After that date, it would incur interest at the standard rate of 24.9%. This is explained in his statement of the same date, on page 5.

His 5 November statement shows that he paid £2,452 between 21 October and 4 November. This paid off most of the balance transfer (some was allocated elsewhere), leaving him with a new balance transfer amount of £473:58 on 5 November. That was wholly paid off in November, but meanwhile interest had been charged from 5 October. £2:21 of as yet unpaid interest appeared on his December statement. This was included in his purchase balance (along with his new purchase of £1,491:44, made on 11 November), to make a total purchase balance of £1,493:65.

3, 5 and 8: Instalment plan 6, the related transaction, and step 3

I regret that my original explanation was not clear enough. What happened was this:

- On 5 December 2022, Mr S's purchase balance was £1,493:65 (as explained above).
- The next day, Mr S spent £1,587:09. That was not added to his purchase balance, but to a separate balance (which I am calling the unstatemented balance).
- On 9 December he created plan 6, for £1,587:09. That reduced his purchase balance by £1,587:09, to nil – with a remainder of £93.44.
- That remainder was deducted from the unstatemented balance, reducing it from £1,587:09 to £1,493:65.
- Between 9 and 29 December, Mr S made four payments which added up to £1,733:16.
- Out of those payments, £580:16 was allocated in steps 1 and 2 to the interest and charges, and to the five instalment plans which already existed on 5 December.
- The rest, £1,153, was allocated in step 3 to the purchase balance first, and then to the five instalment plans. *But as the purchase balance was nil, it all went on the instalment plans.*
- On the next statement date, 5 January 2023, the unstatemented balance became the new purchase balance (minus the £2:21 balance transfer interest) = £1,491:44.

4: What could Mr S have done differently?

If Mr S had not created instalment plan 6, then the purchase balance would not thereby have been reduced by £1,587:09. Then in step 3, £1,153 would have been allocated entirely to his purchase balance instead of to his instalment plans, reducing his purchase balance by over two thirds.

In other words, Mr S should stop creating a new instalment plan as soon as he makes a large purchase. Instead, he should wait for each new purchase to appear on his next statement before moving it into an instalment plan. That way, step 3 will allocate payments in the way that he means it to.

6: The inaccurate statements

The reason why the statements give purchase balances different to what Mr S was expecting is entirely because of the way his payments were allocated in step 3. So this is not a separate issue; they're actually both very much connected with each other.

7: The purchase balances in December and January

The purchase balance on 5 December was £1,493:65 (which consisted of a £1,491:44 purchase and £2:21 of outstanding interest on the old balance transfer). The purchase balance on 5 January was £1,491:44. So they were not identical, because the balance transfer interest had been paid off in the interim.

My final decision

My decision is that I do not uphold this complaint.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr S to accept or reject my decision before 31 May 2024. But this final decision brings to an end our service’s involvement in this complaint.

Richard Wood
Ombudsman