

The complaint

Mr F complains about his mortgage with Mortgage Agency Services Number Five Limited (MAS5). In particular, he says that MAS5 unfairly increased the interest rate on his mortgage, meaning he was overcharged interest over many years. He complains that he's become trapped with MAS5 as a result.

What happened

Mr F took out his mortgage in 2007. He borrowed around £166,000 on interest only terms over 23 years. The mortgage was on an initial fixed rate of 5.89% until 30 June 2009, to be followed by the standard variable rate (SVR). The mortgage was originally with another lender, GMAC-RFC Limited, but was transferred from GMAC to MAS5 shortly after Mr F took it out.

While Mr F was on the fixed rate, the SVR was reduced, but then in 2009 it was increased. The earlier reductions were made in line with changes to the Bank of England base rate. But the 2009 increases – from 2.99% to 3.74% in July and from 3.74% to 4.5% in October – were made even though there were no changes to base rate at those times. Mr F reverted to the SVR on 1 July 2009, the same day that the first of those changes took effect, so he reverted from a fixed rate of 5.89% to an SVR of 3.74%.

MAS5 made further changes to the SVR in 2011 (increasing it to 5.25%) and 2012 (to 5.75%). Again, these changes were made without there being an equivalent change to base rate. After that there were no further changes to the SVR until 2016. Between 2016 and 2022, MAS5 made further changes to the SVR at the same time and by the same amount as changes in base rate. It didn't pass on all the changes to base rate in 2022, but did do so in 2023.

In June 2023 Mr F complained to MAS5. He said that it had unfairly increased the SVR between 2009 and 2012 when there was no reason to do so, in breach of the mortgage terms and conditions. He also said that the SVR was unfairly high because it was higher than the SVR charged by The Co-operative Bank plc – MAS5 is a separate firm to, but wholly owned by, The Co-op.

When he brought his complaint to us, our investigator said that we could only consider the fairness of the interest rate charged in the six years before Mr F complained. But she said that in doing so, she would need to take into account all the changes MAS5 had made, even if they took place more than six years ago, to the extent that they impacted on and were relevant to the fairness of the interest charged within the six year period.

The investigator went on to say that she didn't think it was fair that MAS5 had charged interest within the last six years leading up to Mr F's complaint that took account of the increases in 2011 and 2012. She said that MAS5 should reduce the interest charged from 30 May 2017 (six years before Mr F's complaint was first made) to November 2022 by 1.25%, as if those two increases had never happened. That's because after November 2022 the interest rate was no longer unfair, because MAS5's decisions not to pass on the changes in base rate at that time offset the earlier unfairness. She also said that MAS5 should pay Mr F

£500 compensation.

MAS5 accepted that, and paid the recommended redress to Mr F. But Mr F didn't agree that this went far enough. He said that MAS5 should refund the 2009 increases too – making 2.76% not 1.25%. He didn't think £500 compensation was fair. And he didn't agree that the redress should be limited to the six years before his 2023 complaint.

I've separately issued a jurisdiction decision, in which I concluded that I can only consider the fairness of interest charged for the six years before he complained; that is, from 30 May 2017 onwards. But in doing so I'll need to take account of all the circumstances, including actions by MAS5 before that date, insofar as they're relevant to the fairness of the interest charged from 30 May 2017 onwards. What follows is my findings on the merits of that part of the complaint.

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.

The interest rate charged to Mr F is determined by the mortgage offer and the terms and conditions. The original GMAC mortgage offer said that he would be charged a fixed rate until 30 June 2009, followed by the SVR.

Mr F's mortgage has in fact operated in this way – he has been charged the MAS5 SVR from 1 July 2009 until he redeemed the mortgage earlier this year.

While MAS5 didn't offer Mr F a new interest rate after 2009, it wasn't required to do so and didn't promise that it would. It didn't offer new rates to any customer, so Mr F wasn't treated less favourably than other customers with similar characteristics to him. MAS5 didn't put any barriers – such as an early repayment charge (ERC) – in the way of Mr F moving his mortgage to another lender either. In all the circumstances, I don't think it was unfair that Mr F was charged the SVR rather than being offered a new preferential interest rate.

Mr F has explained that he felt he was trapped with MAS5 and unable to move his mortgage elsewhere, so he had no choice but to pay the SVR. I'm not sure whether or not he explored moving his mortgage to another lender. But if so, and he didn't pass that new lender's criteria, that's not something I can hold MAS5 responsible for. After the expiry of the fixed rate in 2009, there were no barriers – such as early repayment charge – placed in the way of Mr F moving elsewhere.

However, while it wasn't unfair that Mr F was on the SVR, it's important that the SVR itself was set at a fair level – in particular, in the way MAS5 changed it over the years.

After Mr F took out the mortgage, while he was on the fixed rate, MAS5 reduced the SVR significantly in line with changes in the Bank of England base rate. Between 2009 and 2012, it then increased the SVR again – this time at a time when base rate was unchanged.

MAS5's ability to change the SVR is governed by the terms and conditions, which say:

3.1 If the interest rate is the standard variable rate we may vary it for any of the following reasons:

(a) to reflect a change which has occurred, or which we reasonably expect to occur, in the Bank of England base rate or interest rates generally;

- (b) to reflect a change which has occurred, or which we reasonably expect to occur, in the cost of the funds we use in our mortgage lending business;
- (c) to reflect a change which has occurred, or which we reasonably expect to occur, in the interest rates charged by other mortgage lenders;
- (d) to reflect a change in the law or a decision by a court; or
- (e) to reflect a decision or recommendation by an ombudsman, regulator or similar body.

When it increased the SVR between 2009 and 2012, MAS5 relied on condition 3.1 (b) – to reflect a change which had occurred, or which it reasonably expected to occur, in the cost of funds it used in its mortgage lending business.

As I've explained, a complaint about the increases in 2009 and 2011 is out of time – but a complaint about the 2012 increase is not out of time.

And while I can't consider the 2009 and 2011 increases as complaints in their own right, they do form part of all the circumstances relevant to what's fair and reasonable in respect of the interest charged from 30 May 2017 onwards. So I will still need to consider the fairness of those increases insofar as they impacted the interest charged during that period.

MAS5 said that it relied on condition 3.1(b), cost of funds, to increase the interest rate between 2009 and 2012. I've reviewed the evidence MAS5 has provided about this, and I'm not persuaded that MAS5's cost of funds actually did increase at these times – or that it could, at the relevant times, have had a reasonable expectation that such an increase was likely. That's because the way that MAS5 had structured its mortgage lending business meant that it wasn't subject to wider market pressures and so its own funding costs didn't change – even if the costs faced by the wider banking group of which it was a part did.

I'm not therefore persuaded that the contractual basis MAS5 relied on to increase the SVR at these times was valid. Taking that into account, I then need to think about whether it acted fairly and reasonably in all the circumstances in charging the interest that it did during the period I can consider.

In looking at all the circumstances, I think it's relevant to take into account that, as part of the transfer of mortgages – including Mr F's – from GMAC to MAS5, MAS5 agreed that it would maintain the SVR at a level not more than 2% above base rate.

This covenant was between GMAC and MAS5, and Mr F wasn't party to it. It didn't change the terms of his mortgage.

Under the terms and conditions, MAS5 was permitted to vary the SVR for a number of reasons, including to reflect changes to base rate – but it wasn't required to reduce the SVR when base rate reduced. In agreeing to the covenant, MAS5 agreed to restrict its ability to change the SVR beyond that set out in the mortgage terms and conditions.

The result was that, by the time the covenant came to an end in 2009, the SVR had fallen to 2.99%. The SVRs of virtually all other lenders also fell at this time – but they didn't fall to the same extent, because mortgage funding costs didn't reduce by as much as base rate reduced. The result was that, because of the covenant, MAS5's SVR fell by more than it would otherwise have done, and ended up lower than it otherwise would have done, and lower than the SVRs of comparable lenders.

When MAS5 increased the SVR in 2009, it did so from the low level caused by the existence of the covenant. The 2009 increases essentially restored the SVR to what it would have been had the covenant not existed, and had the SVR not reduced as much as it did because of the covenant.

As I say, Mr F wasn't party to the covenant. It was an agreement between MAS5 and GMAC which meant that his interest rate reduced by more than it would have done had his mortgage remained with GMAC, and more than it would have done without the covenant. It meant that his interest rate reduced to a level lower than would have been expected based on the operation of the mortgage terms and conditions alone.

To that extent, the reduction in SVR driven by the covenant benefitted Mr F, because it meant he paid a lower interest rate than he would otherwise have done.

I think that's a relevant factor to take into account when considering whether the later interest rate, charged as a consequence of (among other factors) the 2009 increases was fair. Although MAS5 had no contractual basis for increasing the SVR when it did, those increases corrected for the SVR being at an artificially low level. To require MAS5 to reduce the later interest rate as if those increases had never taken place would be to require it to continue implementing the covenant after it no longer existed, and to implement an interest rate lower than Mr F could have expected by the operation of the terms and conditions of his mortgage alone. I think that would represent over-compensation.

The same considerations don't apply to the 2011 and 2012 increases. The covenant no longer had an impact. So in this respect, I don't think it would be unfair to require MAS5 to reduce the later interest rate as if those increases had never happened.

In summary, therefore, my findings are:

- The increases in 2009 to 2012 are out of time and cannot be considered as complaints in their own right.
- But it wasn't fair and reasonable for the SVR charged after 30 May 2017 to be set at a level which reflected the increases in 2011 and 2012, because there was no contractual basis for those increases and it wouldn't therefore be fair for MAS5 to rely on them in charging interest in the period I can consider.
- But in respect of the increases in 2009, the same doesn't apply – because prior to those increases the SVR was lower than it would otherwise have been, and lower than Mr F could reasonably have expected by operation of the mortgage agreement alone, because of the restrictive covenant. To require MAS5 to reduce the SVR as if the covenant was still in place after 2017 would not represent fair compensation.

To put matters right, MAS5 should refund interest charged as a result of both the 2011 and 2012 increases. That means it should refund 1.25% interest, in respect of interest charged from 30 May 2017 onwards.

In response to the investigator's view, MAS5 said that the refund of interest should only apply until November 2022. That's because between August 2022 and November 2022 it didn't increase the SVR even though the Bank of England base rate increased at those times – which had the effect of removing the lingering unfairness of the 2011 and 2012 increases.

I've thought carefully about this, and I'm persuaded by what MAS5 says. The effect of my redress award is that the MAS5 SVR should have been 1.25% lower than it actually was. I'm

persuaded that if the SVR had been 1.25% lower in 2022, it's likely that MAS5 would have chosen to pass on the base rate increases rather than absorb them – as it would have been entitled to do under condition 3.1 (a). With the redress in place, the SVR would have been lower than many mainstream lenders, and lower than other firms in the wider banking group.

But – as a group – MAS5's mortgages are generally higher risk than those of mainstream lenders and of other parts of the wider banking group. That means they're more likely to go into arrears or default, increasing the costs to MAS5 if that happens.

It's standard practice, and not unreasonable, to include an element of "pricing for risk" in setting interest rates. While the terms and conditions don't allow MAS5 to increase the interest rate for this reason, they do allow it to increase the interest rate to reflect changes in base rate. I'm satisfied that if the interest rate had been 1.25% lower – as is the case following my redress award – then MAS5 would have passed on the base rate increases, as it would have been entitled to do.

Therefore, to require MAS5 to continue the interest rate refund beyond November 2022 would require it to treat Mr F's mortgage as if the 2011 and 2012 increases had never happened, and also as if the 2022 base rate cuts had not been passed on. I don't think it's likely that his mortgage would ever have been in a position where both those things happened, and therefore to require MAS5 to do that would be over-compensation.

I do understand the impact recent interest rate rises have had, and the difficulty that caused Mr F until he redeemed the mortgage earlier this year. However, that's driven by recent economic conditions. MAS5 has increased the SVR to reflect changes in base rate, as it's entitled to do under the terms and conditions, and the result is not out of line with that of other comparable lenders. I don't think there's any basis on which I can fairly ask it to reduce the interest rate charged after November 2022.

MAS5 have offered to re-work Mr F's mortgage account by reducing the rate on the mortgage by

- 1.25% from 30 May 2017 to 30 August 2022;
- 0.75% from 1 September 2022 to 31 October 2022;
- 0.25% from 1 November 2022 to 30 November 2022.

The gradual change in the rate is a result of the timings of the changes MAS5 said it would have made had the rate been 1.25% lower before 2022. This reflects the fact that base rate increased by 0.5% in August and September 2022 – neither of which were passed on but would have been had the rate been lower.

As I've explained, I'm satisfied that this is what MAS5 would have done, had it not been charging Mr F an unfairly high rate prior to 2022. And so I'm satisfied the offer it's now made puts Mr F back in the position he would have been in, had MAS5 applied a fair rate of interest from 30 May 2017.

Finally, I do think that the additional interest paid by Mr F between May 2017 and November 2022 had a substantial impact on him. He's explained that it caused him substantial stress and worry – though I also note that the mortgage didn't go into arrears at any point over this period and Mr F was always able to repay in full. In setting the level of compensation, I take into account the impact of what went wrong on Mr F, and from the evidence I've seen I'm satisfied £500 is fair compensation.

Putting things right

I've set out above my conclusions on this complaint. I understand that, following the investigator's view, MAS5 has already paid the compensation she recommended to Mr F by way of an interim payment while his case was considered by an ombudsman – refunding the additional interest charged over the years, plus 8% simple interest on each overpayment, plus £500 compensation. As I've reached the same view, I don't require MAS5 to make any further payment to Mr F.

My final decision

My final decision is that I uphold this complaint and direct Mortgage Agency Services Number Five Limited to pay compensation to Mr F on the basis I've set out above. On the basis that it has already done so, I don't require it to take any further action.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr F to accept or reject my decision before 12 July 2024.

Simon Pugh
Ombudsman