

## **The complaint**

This complaint's about an interest-only mortgage that Ms B holds with Bank of Scotland plc trading as Birmingham Midshires (BM). The mortgage started in 2007 with a five-year term, so was initially due to expire in 2012. It's been extended since then, but the final extension expired in December 2021, since which time BM has been seeking Ms B's proposal for repaying the overdue balance. Ms B hasn't yet repaid the mortgage; she's continued to make regular monthly payments by direct debit.

However, interest rates have been rising since the mortgage expired, and because BM doesn't recalculate monthly instalments on expired mortgages, the monthly direct debit amounts have stayed the same while the interest charged has gone up. The resulting shortfall has increased the outstanding balance, which Ms B is unhappy with. BM started legal action to enforce its security, which is on hold while we look at the complaint.

## **What happened**

The broad circumstances of this complaint are known to Ms B and BM. I'm also aware that the investigator issued a comprehensive response to the complaint, which has been shared with all parties, and so I don't need to repeat the details here.

Our decisions are published, and it's important that I don't include any information that might result in Ms B being identified. Instead I'll focus on giving the reasons for my decision. If I don't mention something, it won't be because I've ignored it. It'll be because I didn't think it was material to the outcome of the complaint.

## **What I've decided – and why**

I'll make some general observations before dealing with the substance of the complaint. We're not the regulator of financial businesses, and we don't "police" their internal processes or how they operate generally. That's the job of the Financial Conduct Authority (FCA).

We deal with individual disputes between businesses and their customers. In doing that, we don't replicate the work of the courts. We're impartial, and we don't take either side's instructions on how we investigate a complaint. We conduct our investigations and reach our conclusions without interference from anyone else.

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

Where the evidence is incomplete and/or contradictory, I'm required to reach my decision on the basis of what I consider is most likely to have happened, on the balance of probabilities. That's broadly the same test used by the courts in civil cases.

My starting point here is that Ms B borrowed money from BM, and under the terms of the original agreement, was due to repay the money in 2012, but following at least two term extensions, by December 2021 at the latest. No-one is entitled to borrow money; and even when they've borrowed before, they're not automatically entitled to more time to repay the

debt after it has fallen due. But a lender must treat customers fairly. In the context of an application for a term extension, that means assessing it fairly in accordance with the bank's lending criteria and being mindful of what mortgage regulation requires of it. Lenders' criteria are commercially sensitive and not typically made public.

There are regulations in place that have flowed from the Mortgage Market Review (MMR) carried out by the Financial Conduct Authority (FCA) which took place after the financial crash in 2008. This has led to a series of major changes, effective since 2014, in the way residential mortgages are regulated. MMR regulations have brought about requirements for stricter lending assessments, aimed at protecting consumers and encouraging mortgage lenders to act more responsibly.

The FCA recognised though that existing borrowers who wanted to make changes to their mortgages might have difficulties with this if they had passed tests under the old rules but wouldn't under the new ones. So, it introduced certain rules to address this. The rules are contained in the Mortgages and Home Finance: Conduct of Business Sourcebook (MCOB).

MCOB says a lender doesn't have to carry out an affordability assessment if a borrower wants to vary or replace an existing mortgage and there is no additional borrowing (other than for product fees) and no change to the terms of the mortgage that is material to affordability

There are also transitional arrangements which say that a lender need not carry out an affordability assessment if:

- the borrower has an existing mortgage taken out before 26 April 2014, and is applying to vary that mortgage or replace it with a new one;
- the application wouldn't involve any additional borrowing except for essential repairs to the property, or to add product fees to the balance;
- there's been no further borrowing (with some exceptions) since 26 April 2014; and
- the proposed transaction is in the borrower's best interests.

So, under this rule, even where a change material to the affordability of the mortgage takes place, the lender can, *if it chooses*, waive an affordability assessment. If the lender decides to carry out an affordability assessment, it shouldn't use that as a reason to decline an application if allowing the application would otherwise be in the customer's best interests. But the lender can take the assessment into account as part of its consideration of best interests.

This means there are two routes that an application for an existing borrower can go down. If there's no change to the terms of the mortgage contract material to affordability, there's no obligation to carry out an affordability assessment at all. And if there is a change to the terms of the mortgage contract material to affordability, a lender could still decide to allow an application without an affordability assessment if doing so would otherwise be in the borrower's best interests.

The above provisions apply to regulated mortgages only; the offer document for Ms B's mortgage doesn't specify if it was regulated or unregulated, but given that it was secured on a property that wasn't Mrs B's home, it seems more likely that it is an unregulated mortgage. However, I have given Ms B the benefit of the doubt by taking into account the MMR provisions of 2014 when assessing how this complaint should fairly be resolved.

The first term extension was in 2012, so pre-dated the new provisions; it was for five years so ran out in 2017. For any new extension after that, the 2014 provisions would have been a

relevant consideration if the mortgage was regulated. A term extension *is* a material change to the mortgage contract. In the circumstances, when assessing any term extension BM was, I find, entitled to consider affordability. But it also had to consider whether the change to the mortgage would be in Ms B's best interests – and if it was, then the affordability assessment could be disregarded.

In fact, what happened, between 2017 and 2021, was that BM's computer system simply extended the term automatically. BM had a number discussions with Ms B throughout this period, during which the details and schedule of her strategy for repaying the debt varied from time to time, albeit the fundamental intention was always that it would be by selling the mortgaged property, which isn't Ms B's home, once it had been refurbished.

The difficulty here, however, is that Ms B's timetable for refurbishing and marketing the property has kept being put back, and in 2021, when the mortgage migrated to a new computer system, BM stopped renewing the mortgage automatically and decided to insist it be repaid. We're now close to three years on from that point, and even now, Ms B is still talking about when she aims to put the property up for sale. In all the circumstances, I consider that BM has been more than fair to Ms B and shown a high degree of patience and forbearance over repayment of the overdue mortgage balance.

As far as the monthly interest payments are concerned, it's normal for a lender to vary the amounts collected under a direct debit on a "live" account; that is to say, live in the context of a mortgage that is still within its contractual term. However, Ms B's mortgage isn't a live account in that context; it's an expired mortgage where the entire debt is overdue for repayment. In those circumstances, I don't consider it unfair treatment if the business' accounting system no longer changes the amount collected under the direct debit when the interest rate changes. The idea of a contractual monthly payment no longer applies when a contract has expired.

I've seen examples of correspondence BM sent Ms B throughout the period since the mortgage expired. I'm satisfied Ms B was on notice that she owed BM the entire mortgage debt, and could pay any amounts at any time, regardless of what was happening with the direct debit. She recently began making lump sum payments in addition to the amounts collected each month. In my view, that was something Ms B could have done at any time after the monthly interest being charged began to exceed the amount being collected under the direct debit.

That begs the question of what happens next. BM paused recovery action whilst the case has been with us. I think it is also important to explain here that lenders will generally agree to put recovery action on hold whilst we look at a complaint, but they don't have to and we can't force them to.

If the Financial Ombudsman Service had that power it would undermine our impartiality between the parties to a complaint. It would also create the potential for consumers to use our service to bring complaints with the intention of having any legal action put on hold, thereby obstructing businesses that were trying to take action through the courts to recover money legitimately owed by the consumers.

I do not wish to alarm Ms B but I would not want her to be under any misunderstanding that we would tell BM that it must delay recovery action afresh in the event of any new complaint being raised about the mortgage. It is a matter for a court to decide whether it is appropriate to adjourn or suspend any legal action, not this service.

**My final decision**

My final decision is that I don't uphold this complaint or make any order or award against Bank of Scotland plc trading as Birmingham Midshires.

My final decision concludes this service's consideration of this complaint, which means I'll not be engaging in any further consideration or discussion of the merits of it.

Under the rules of the Financial Ombudsman Service, I'm required to ask Ms B to accept or reject my decision before 21 August 2024.

Jeff Parrington

**Ombudsman**