DRN-4869541

The complaint

Ms S and Mr S complain that Kensington Mortgage Company Limited wouldn't offer them a new interest rate product on their mortgage and that it gave them conflicting reasons about why it wouldn't do so.

What happened

Ms S and Mr S took out their mortgage with GE Money Home Lending Limited (trading as First National) in 2008. They borrowed £170,995 plus fees on an interest-only basis over a term of 30 years.

A fixed interest rate of 8.14% applied to the mortgage for the first 24 months and, after that, a variable rate of 3.39% above the Barclays Bank Plc Base Rate for the rest of the term. The mortgage was transferred from GE Money to Kensington in 2016.

In April 2022, Ms S was worried about rising interest rates, so she contacted Kensington to ask whether she could move the mortgage onto a fixed interest rate. Kensington told her that it didn't offer new interest rate products directly to customers.

In September 2022 Ms S contacted Kensington again to ask for a fixed interest rate. She says she did so because she had found out that Kensington did in fact have new interest rate products available to existing customers. Kensington told her it couldn't offer a new rate on her and Mr S's mortgage. It then told her that product switches were only available to customers whose mortgages had originally been taken out with it – which didn't include Ms S and Mr S, because they had originally taken out their mortgage with GE Money.

Ms S said that she was a 'mortgage prisoner' and rising interest rates were making the mortgage unaffordable. She also consulted a mortgage adviser, but they found she wasn't eligible to re-mortgage to another lender. In November 2022 she complained to Kensington.

Kensington said it couldn't offer a new interest rate product on the mortgage. It suggested Ms S and Mr S take independent financial advice. It also said it could review their circumstances to see what it could do to help if they were finding their mortgage payments difficult to manage.

Ms S and Mr S asked the Financial Ombudsman Service to look into their complaint. Our Investigator recommended that the complaint should be upheld. She concluded that Kensington should have allowed Ms S and Mr S to take a fixed interest rate product when Ms S asked for one in April 2022. She recommended that Kensington provide Ms S and Mr S with details of the interest rate products it had available at that time, allow them to choose one, re-work their mortgage on that basis, and refund any resulting overpayments they had made plus 8% simple annual interest. She also recommended that it pay them an additional £300 compensation.

Kensington didn't accept that conclusion and asked for an Ombudsman's review. It said, in summary:

- the terms and conditions of Ms S and Mr S's mortgage remained the same after the transfer from GE Money, and under those terms it didn't have to offer Ms S and Mr S a new interest rate product;

- in declining Ms S and Mr S's request for a new fixed interest rate it had treated them the same as any other customer with an outstanding fees balance and in line with its usual criteria;

- Ms S and Mr S's mortgage also didn't meet its criteria for a new product because the "reversionary margin on a new product cannot be higher than the one a customer's mortgage is currently on";

- the securitization of the mortgage wasn't the reason it didn't offer a new product. The reason was that Ms S and Mr S's mortgage didn't meet its criteria.

Ms S and Mr S didn't say whether or not they accepted the Investigator's recommendation, but they said they didn't know anything about any arrears on the mortgage and they would have paid the 93p arrears Kensington had referred to straight away if it had told them this was outstanding.

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.

Lenders aren't obliged to offer new interest rate products to their customers. A lender might legitimately choose not to offer rates to any customers. Where it does offer rates, it's fair and reasonable – and standard practice in the mortgage industry – for a lender to have eligibility criteria. These criteria might mean that not all borrowers are offered the same rate, or that some are not offered a rate at all, based on things like loan to value and arrears history.

In this case, Kensington has given various different reasons for refusing Ms S and Mr S a new interest rate, as I have summarised above.

Kensington initially refused Ms S and Mr S a new rate because it said it doesn't offer interest rate products directly to its customers. It said that any rates Ms S had seen online were for new lending (new customers) and that Ms S would need to speak to a broker or independent financial adviser if she wanted to apply for a new rate. However, Kensington's later responses to Ms S – and indeed its response to this Service – contradict this. Kensington does offer new interest rate products to existing customers directly if they meet its criteria.

Kensington then refused Ms S and Mr S a new rate because their mortgage originated with GE Money, and it said that under GE Money's terms and conditions it wasn't obliged to offer new interest rate products. Mortgage terms and conditions don't generally require the lender, or its successors, to offer new interest rate products – but they don't prohibit new products being offered either, and the terms of Ms S and Mr S's mortgage are no exception. I don't think that the real reason Kensington wouldn't offer a new product on Ms S and Mr S's mortgage was because of what the terms and conditions said. I think it was because theirs was originally a GE Money mortgage and, as part of its business model, Kensington securitizes its mortgages. This means it offers the beneficial interest in groups of loans to third party investors to raise funds for its ongoing mortgage business. This is a normal and legitimate feature of the mortgage industry, and it's not inherently unfair that Kensington operates its business in this way.

However, the Financial Ombudsman Service has in other cases taken the view that it's unfair for borrowers to be refused a new rate because of this, where the borrower can't move their mortgage to another lender or shop around for a better rate. I think Ms S and Mr S are likely to be in that position: they have an interest-only mortgage, and Ms S has told us that she has spoken to an independent mortgage adviser but they couldn't find a mortgage with another lender due to concerns about affordability.

So if Kensington were to say that Ms S and Mr S must remain on their current mortgage deal, because of the way it has chosen to securitize this mortgage, and that in turn was based on when and how they took their mortgage out around 14 years before Ms S asked about a rate in 2022, I would, in all the circumstances, consider this not to be a fair and reasonable basis on which to refuse them a new interest rate. Refusing Ms S and Mr S a new rate on this basis wouldn't be because of current characteristics of Ms S and Mr S or their mortgage – such as loan to value or arrears, or their wider credit risk.

The rules of mortgage regulation, which are found in the Financial Conduct Authority (FCA) Handbook under the heading MCOB, are relevant here. In particular, MCOB 11.8.1 E (the E means it's an evidential provision, not a rule) says that where a borrower is unable to move their mortgage to a new lender (as Ms S and Mr S were), their existing lender:

> should not (for example, by offering less favourable interest rates or other terms) take advantage of the customer's situation or treat the customer any less favourably than it would treat other customers with similar characteristics. To do so may be relied on as tending to show contravention of Principle 6 (Customer's interests).

Principle 6 is another part of the FCA Handbook, and says that a firm:

> must pay due regard to the interests of its customers and treat them fairly

As I've already said, securitization is not an unusual business model and not inherently unfair. However, this is not something Ms S and Mr S were aware of or had any control over. And I don't think it can be said to amount to a characteristic of them or their mortgage – it's something done to their mortgage by Kensington.

I don't therefore consider that Kensington's choice to manage its business in this way is a relevant consideration for the purposes of the comparison envisaged by MCOB 11.8.1 E. It's a matter for Kensington's commercial judgement how it chooses to structure its business. But if – as I think is the case here – that results in unfairness in an individual case, that's a matter for me.

In my view, what's relevant is whether, when Ms S asked for a new rate, she and Mr S had similar characteristics to other borrowers who would be eligible for a new interest rate – and whether, if they did, refusing them a rate would tend to show unfairness of the sort envisaged by MCOB 11.8.1 E.

Kensington has provided details of its eligibility criteria and said that Ms S and Mr S don't meet some of them. They are:

- no arrears or other amounts due;
- new interest rate must be lower than current interest rate;
- "reversion margin" on the new product must be less than the current interest rate.

The transaction history for Ms S and Mr S's mortgage shows an overdue balance of £20 when Ms S initially asked for a rate switch in April 2022. This relates to two unpaid direct debit fees, each of £10, which were applied to the mortgage in 2019. This amount is not, however, showing on either the July 2021 or the July 2022 mortgage statement. An overdue balance of 93p is showing on the July 2022 statement – but the statement shows the mortgage was also in credit by £40.40.

I haven't seen copies of any correspondence that Kensington sent Ms S and Mr S to let them know there was an overdue balance that needed to be paid. Given how small these amounts are, I think it likely that Ms S and Mr S would have paid them had they been asked to do so. In any event, the mortgage was in credit by more than either of the amounts Kensington claims were overdue. In the circumstances, I don't think that this overdue balance is grounds on which it was fair for Kensington to refuse Ms S and Mr S a new rate.

The information Kensington has given us about its available rates shows that Ms S and Mr S didn't meet the "reversion margin" requirement in April 2022. The interest rate on their mortgage at the time was 3.89% and the reversion margin for Kensington's available fixed interest rate products was 4% or more.

However, this is something that will vary over time and is dependent on Kensington's changing offering – and I find it difficult to see its relevance. Ms S and Mr S might be prepared to take the risk of a higher reversion rate in future in return for the certainty of a fixed rate now. They might also, of course, subject to eligibility and availability, choose to take another new fixed rate in future before a reversionary rate on a new product takes effect. So I don't think the fact that this mortgage didn't meet this criterion at the time Ms S asked for a new rate was a fair and reasonable reason to refuse her, bearing in mind the particular circumstances – which included that the mortgage had been on a variable reversion rate for many years and Ms S was very concerned about that rate increasing.

Kensington has estimated the loan to value of the property at 76% in April 2022. The information it has provided about its available fixed interest rate products indicates that the lowest fixed rate it was offering in April 2022 at 80% loan to value was 3.46% for two years – lower than the 3.89% Ms S and Mr S were paying when Ms S initially asked about taking a new interest rate product on 4 April 2022. Ms S has referred to some other interest rate products she saw Kensington was offering in April 2022, but they appear to have been for new customers rather than existing borrowers.

If Kensington had treated Ms S and Mr S fairly when Ms S asked for a new rate on 4 April 2022, they would have been able to decide whether to take a rate at the time of asking and if so which one. In the circumstances, I think they are very likely to have chosen to take a fixed rate in April 2022, both to reduce their interest rate and to protect them against potential future interest rate rises on their existing variable rate. I think that they should have had the opportunity to do that. I don't find that Ms S and Mr S should have been refused a fixed rate for the various reasons Kensington has given – some of which are clearly contradictory. In all the circumstances, therefore, I am satisfied that in refusing Ms S and Mr S a new rate, Kensington didn't act fairly and reasonably.

I therefore find that Ms S and Mr S should fairly have the opportunity to take one of the fixed interest rate products Kensington had available on 4 April 2022 if they wish to do so, subject to relevant loan to value criteria. They may wish to seek independent advice first if necessary.

Finally, I recognise that this matter has caused Ms S and Mr S worry and upset. Ms S has explained the difficulty increasing interest rates have caused as the monthly mortgage payments have increased significantly. She's said she's had to rely on credit cards for essential household expenditure and her health has been affected by the worry about the situation. I can see that Kensington's communication with her about this matter has added to this and she has found it very frustrating. I've thought carefully about this, and I agree with our Investigator that an award of £300 is fair and reasonable in recognition of the impact on Ms S and Mr S of Kensington's treatment of them.

Putting things right

To put things right, Kensington should give Ms S and Mr S the option of being put in the position they would have been in had it offered them a rate when they asked on 4 April 2022. Allowing time for an application to proceed, if Ms S and Mr S accept this option, it should rework their mortgage as if a new interest rate product had been in place from 1 June 2022.

Kensington should provide Ms S and Mr S with a list of the rates it had available in April 2022. If Ms S and Mr S choose to accept one of those rates, Kensington must re-calculate their mortgage on that basis.

If Ms S and Mr S accept one of those rates and it would have ended before the date of my final decision, Kensington should also provide them with a list of the rates it had available at the end date of the rate they have accepted, and give them the option of accepting one of those as well, again subject to relevant loan to value and other criteria.

Ms S and Mr S may choose whether to have the overpayments they have made on the variable mortgage interest rate they have been paying either refunded to them or left on the mortgage as a reduction to the capital mortgage balance. If they choose to have the overpayments refunded to them directly, Kensington should also pay them 8% simple annual interest from the date of each monthly overpayment to the date of settlement.

Kensington should give any future application for a new rate fair consideration according to its criteria at that time, taking into account MCOB 11.8.1 E if it is still relevant at that time.

Kensington should also pay Ms S and Mr S £300 compensation.

My final decision

For the reasons I've given, my final decision is that I uphold this complaint. Kensington Mortgage Company Limited must:

- provide Ms S and Mr S with a list of the rates it had available in April 2022;
- if Ms S and Mr S choose to accept one of those rates, Kensington should re-work their mortgage on that basis, backdated to 1 June 2022;
- where the re-work results in an overpayment having been made, give Ms S and Mr S the option of either:
    - the overpayment being refunded to them directly, plus simple annual interest of 8%* running from the date of each monthly overpayment to the date of settlement; or
    - the overpayment being used to reduce the balance of the mortgage, and therefore the amount of future interest charged;
- if Ms S and Mr S accept a rate to be backdated to 1 June 2022 and that rate comes to an end before the date of this final decision, Kensington should provide them with a list of the rates it had available at the end date of the rate it has implemented with effect from 1

June 2022, allow Ms S and Mr S to accept one of those rates and re-work the mortgage backdated to the end date of the first rate they have chosen. It should then refund any overpayments or leave them on the mortgage to reduce the balance, whichever Ms S and Mr S choose, and add simple annual interest at 8% on any overpayments it refunds running from the date of each overpayment to the date of settlement. If however this results in an underpayment Ms S and Mr S will need to make arrangements to pay this;

- pay Ms S and Mr S £300 compensation.

*Kensington may deduct income tax from the 8% interest element of my award as required by HMRC. But it should tell Ms S and Mr S what it has deducted so they can reclaim the tax from HMRC if they're entitled to do so.

Under the rules of the Financial Ombudsman Service, I'm required to ask Ms S and Mr S to accept or reject my decision before 15 October 2024.

Janet Millington
Ombudsman