DRN-4988207

Financial Ombudsman Service

**The complaint**

Mr A complains that Lloyds Bank PLC misled him about the interest he would pay on his mortgage during a six month interest only period. He says that he's been overcharged interest as a result.

**What happened**

Mr A has a mortgage with Lloyds. In August 2023, he asked Lloyds for help managing his monthly payments because his interest rate was about to increase. Lloyds said he could switch his mortgage to interest only terms for a six month period, in line with the concessions to help borrowers set out in the government's mortgage charter.

At the time, Mr A was on a fixed interest rate of 1.52%, but the fixed rate was due to expire on 31 October 2023. Mr A says that Lloyds told him that if he took the six month interest only period starting in October he would be charged interest at 1.52%, but if he took it in November he would be charged the higher standard variable rate (SVR), then around 8%. So Mr A applied in September to start the interest only period in October.

In November, his fixed rate came to an end and his mortgage reverted to the SVR, which was then 8.74% – meaning the amount of interest charged each month increased. But Lloyds kept the monthly payments the same. This meant Mr A was now not paying enough each month to cover the interest being charged. The excess interest was added to the mortgage balance. As a result, by the time the interest only period ended, the balance had increased significantly.

In March 2024 Lloyds wrote to Mr A setting out what his new balance was, and what the new monthly payments would be, following the end of the arrangement.

Mr A then took a new interest rate. He chose a tracker rate of 0.64% above Bank of England base rate for two years, meaning his new interest rate was 5.89%. He also complained.

Mr A said it was not made clear to him that extra interest would be charged and added to his balance when he agreed to the arrangement. He understood that his payments and interest rate had been fixed for the whole of the six month period. He said that meant his mortgage balance and loan to value had increased, which affected the choice of new interest rates available to him. He said that Lloyds knows he is dyslexic and struggles with complex financial information, and it should have done more to explain things to him.

Lloyds made an offer to resolve Mr A's complaint. It said that it had listened to a call Mr A had with a Lloyds adviser on 29 August 2023. Mr A had been given correct information on that call – that his payments would stay the same throughout the six month period, even if the interest rate changes, and that at the end of the six months Lloyds would tell Mr A what his new monthly payment would be. It said adding the additional interest to the loan balance hadn't significantly changed the loan to value or the new fixed rates Mr A now qualified for.

But Lloyds said that it would offer Mr A the best interest rate that would have been available to him had he switched rates in August 2023. It offered him the choice of a two year fixed rate of 5.70%, a three year fixed rate of 5.01%, or a ten year fixed rate of 4.83%. Lloyds said that if Mr A selected one of those rates it would backdate the rate to 1 November 2023 and reduce the balance of his mortgage as if he'd been charged that rate rather than the SVR from then on. Or he could choose to remain on the tracker rate he'd selected in March 2024, in which case his balance would stay the same.

Our investigator thought that was a fair offer to resolve the complaint. Mr A didn't agree. He said his mortgage balance had increased substantially. He was told on the phone that his interest rate would stay fixed at 1.52% for six months. He said that if he had known so much extra interest would be added to his mortgage balance he would have taken a new interest rate at the time. He asked for an ombudsman to review his 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.

I can understand why Mr A was so concerned about what would happen when his interest rate expired. He had looked online for new interest rates and even taking a new fixed rate would increase his monthly payments by around £1,000 – moving onto the SVR would be even more expensive. So Mr A got in touch with Lloyds to see what his options were.

*What Lloyds said*

I've listened to the call Mr A had with Lloyds on 29 August 2023. He said his interest rate was coming to an end and he had looked at new rates online but they were much higher, so he asked whether there was anything Lloyds could do to help.

Lloyds said it had no other rates available but Mr A could speak to a mortgage adviser if he wanted to make any other changes. Mr A asked about converting to interest only. Lloyds said that he would need to speak to an adviser, and meet Lloyds' criteria, to switch to interest only permanently. But he could switch to interest only for six months online. It said that it would be

> "six months payments on your existing rate, and then any changes in your interest rate in the meantime would be factored in when your mortgage monthly payment is re-calculated at the end of the six month period."

Mr A said he didn't understand that. By way of further explanation, Lloyds said

> "your monthly payment would be fixed for six months based on your interest rate as it is today. During that six month period, if your interest rate changed, your monthly payment will still stay the same for the six months, but then at the end of the six months we will write out to you to tell you what your new monthly payment will be based on what hasn't been paid for the six months and changes in the rate in the meantime."

Mr A asked if this meant his mortgage would stay at the same rate for the six months, or go up to a higher rate. Lloyds said

> "unless your interest rate is due to change next month, which it's not, your monthly payments on interest only would be based on the rate that you're currently on, so what I'm saying is if your interest rate changes in the meantime that would just be factored in when we write out to you to make you aware of what the new interest rate and what the new monthly payment will be when the interest only period comes to an

end."

Mr A said

> "I'm with you. So I can fix on my 2.19% now for six months?"

Lloyds said:

> "Currently you're on 1.52%. You can fix on interest only on that rate for six months. Then as I say at the end of the six months we'll write out to you to make you aware of what the new monthly payment will be, because it will go up, it will be higher than what you're currently paying after the six month period."

There was some further discussion, and Lloyds again confirmed that the six month interest only period would be based on the interest rate in the month Mr A applied.

Mr A also repeatedly explained that he is dyslexic and struggles with using websites, and asked whether it was possible to apply over the phone. But Lloyds said it could only be done via the website, so eventually Mr A said he would ask someone to help him manage it online. Lloyds also didn't ask whether Mr A needed any adjustments in how it writes to him, including letters confirming how the six month interest only switch would operate.

Mr A rang back on 20 September 2023. He said he applied for the interest only period online. He wanted to check when his current interest rate deal ended, so that he could make sure he only went on to interest only at the end of his deal. He said he understood from the previous call that if he applied before his old rate ended the six months would be at that interest rate. Lloyds said it would start from the payment due at the end of October because he had applied in September. Mr A asked if it could be moved to start in November, but Lloyds said this wasn't possible.

Lloyds wrote to Mr A to confirm the arrangement. In the letter, it said:

> **"Arrangement Summary**
>
> - Your arrangement will start from 1 October 2023
> - Your monthly payments during the arrangement will be £453.35
> - Your arrangement will last for six months.
>
> …
>
> These payments are fixed for 6 months. Even if the interest rate that applies to your mortgage changes, these payments won't – until the arrangement ends. If your interest rate goes up, the monthly payments during the arrangement won't cover all the interest being charged. We'll add the difference to your mortgage balance. There's more about this in the "**Helpful information – things you need to know"** section at the end of this letter."

The "helpful information" section included the following questions and answers:

> **"What happens if my interest rate changes during this arrangement?**
>
> Your payments won't change while the arrangement is in place. We work out your lower monthly payments using your mortgage balance and interest rates at the start

of the arrangement.

But the interest rate applied to your mortgage can change.

**Why could my interest rate go up, and what will happen if it does?**

You might be on a fixed rate that's going to end while the arrangement is in place. Or you could be on a tracker rate that goes up because the Bank of England base rate goes up.

If this happens and the rate applied to your mortgage balance goes up, the arrangement won't change. You'll still pay the same amount during the arrangement period.

If your interest rates go up, the amount you're paying won't cover all the mortgage interest. We'll add any interest you don't pay off with your lower monthly payment to your mortgage balance. This means that the total amount you'll pay over tour mortgage term will be more, as your mortgage balance will be higher.

At the end of the arrangement, we'll increase your monthly payment to cover your higher balance. We'll write to you before it's due to change."

*What actually happened*

When Mr A took the six month interest only period, Lloyds fixed his monthly payments as at the time he applied. When he applied in September, he was still on the fixed rate, paying interest of £453.35 per month (and also paying some capital back). So Lloyds fixed his monthly payments at that level for the six months of the interest only period – meaning he would then only pay £453.35 in interest, but no capital.

But Lloyds only fixed the monthly payments – not the interest rate. Mr A's interest rate hadn't changed – which meant he was still going to be charged 1.52% in October, and then the SVR of over 8% from November onwards.

What this meant was that from November 2023 to March 2024, Lloyds was *charging* Mr A over 8% interest, but only asking him to *pay* 1.52%. What usually happens with an interest only mortgage is that the monthly payment covers the interest charged, so the balance stays the same. But because Lloyds fixed the monthly payment at the lower level but still allowed the interest rate to increase, Mr A wasn't paying enough to cover the interest for the last five months of the interest only period. The extra interest charged was added to the mortgage balance.

*Did Lloyds act fairly?*

I don't think it did. Treating Mr A's mortgage in this way wasn't necessarily wrong – the problem was that Lloyds didn't make sure Mr A understood what was happening. And that meant he didn't have enough information to decide what to do next.

In saying that, I've taken into account the Consumer Duty as well as the rules of mortgage regulation. One part of the Consumer Duty says that Lloyds needs to make sure it gave Mr A clear, fair and not misleading information so that he could make timely and effective decisions. Another part says it needs to support him to achieve his financial objectives. Lloyds also needs to avoid foreseeable harm. And when it has any interaction with Mr A, it needs to make sure that he understands what is happening, checking his understanding if necessary.

Mr A's objective was to mitigate the impact of increasing interest rates. He was coming to the end of a low fixed rate, and was concerned that new fixed rates were much higher. He was worried he might not be able to afford the monthly payments on a new interest rate.

Lloyds ought to have explained to him that if he took the six month interest only arrangement, only his monthly payments – not the interest rate – would be fixed. So while Mr A wouldn't be asked to pay a higher monthly payment for six months, he would still be charged a higher amount. The difference between the interest he was charged and the interest he was paying would be added to his mortgage balance.

But Lloyds didn't make that clear in the phone calls. It gave the impression that his interest rate would be fixed for six months. It didn't explain that extra interest would be added to his mortgage balance. This means that Lloyds didn't give him enough information to understand what would happen, or to make an informed decision about what to do.

While the later letter did explain things more clearly, I don't think that was enough. Firstly, it only explained what would happen in general terms. It didn't give specific figures to allow Mr A to understand the impact on his own mortgage. Secondly, that letter was sent after Mr A had applied for the interest only period, confirming it had been put in place – so it didn't give Mr A the information he needed before making the decision to help him decide whether to go ahead. And thirdly Lloyds didn't take into account what Mr A had said about his dyslexia in the way it communicated this to him.

At the point at which he decided to apply for the six month interest only period, Mr A – wrongly – thought his interest rate (not just his payments) would be fixed for six months. It was that which led him to decide to go ahead. Lloyds didn't give him the clear, fair and not misleading information he needed to make a timely and effective decision. It also meant that Mr A didn't consider taking out a new interest rate at that point rather than going on to the SVR between November and March – which was foreseeable harm.

Lloyds ought to have made clear that Mr A had three choices:

1) He could take a new fixed rate to follow on from his old one without taking a six month interest only period. This would mean his mortgage balance didn't increase, but his monthly payments would go up by around £1,000 a month.

2) He could take a new fixed rate and also take the six month interest only period. If he applied for the six month interest only period in September, his payments for the six months would be fixed at £453 based on the 1.52% interest rate but the interest charged would increase from November, adding around £1,000 per month in interest to the mortgage balance for each of the last five months.

3) He could choose not to take a new fixed rate and take the six month interest only period. If he applied in September, his payments would be fixed at £453, but interest at the standard variable rate of 8% would be charged from November onwards – meaning around £1,900 of extra interest would be added to the mortgage balance for each of the last five months. This option is the most expensive in terms of the impact on Mr A's mortgage balance – but does mean he had the chance of waiting to see if new interest rate deals were lower by early 2024 than they were in August 2023.

Lloyds didn't explain that by taking the interest only period Mr A would still be charged higher interest even if he wasn't paying it, and didn't explain that he could take a new fixed rate too. This meant that Mr A was given option three – without knowing that this is what would happen, and without knowing he had the choice of the other options too.

What ought to have happened is that Lloyds ought to have explained all this to Mr A – before he decided not to apply for a new fixed rate and to take the six months on interest only. If it had done so, he could have made an informed decision about which option to take.

To put things right, therefore, Lloyds should put Mr A back in the position he would have been in had it given him enough information at the time.

Realistically, I don't think Mr A would ever have taken option one. He was too concerned about the impact of rising interest rates not to have tried to reduce his payments in some way. But, had he understood what was on offer and how Lloyds would treat his mortgage, he might have taken option two.

When Mr A complained, Lloyds offered to allow him to pick a fixed rate from the list of those available in August 2023, and to re-calculate his mortgage as if that rate had been put in place at the time. It only offered fixed rates because it didn't have any tracker rates available in August 2023.

I think that's a fair offer. Lloyds' failure to explain things properly at the time means that Mr A ended up with option three. Lloyds is now offering him the chance to have taken option two instead – making sure that his mortgage balance and monthly payments are what they would have been if he had made that choice at the time.

That means that Mr A now has a choice:

- He can leave things as they are – with his mortgage balance based on
    - Interest at 1.52% for October 2023
    - Interest at the SVR of 8.74% for November 2023 to March 2024, with the amounts above £453 added to his mortgage balance
    - Interest at the tracker rate he selected in March 2024 for two years from then (5.89% in March 2024, since reduced to 5.39%).
- Or he can accept Lloyds' offer – with his mortgage balance based on
    - Interest at 1.52% for October 2023
    - Interest at 4.83%, 5.01% or 5.70% for November 2023 to March 2024, with the (lower) amounts above £453 added to his mortgage balance
    - Interest at one of 4.83% for ten years, 5.01% for five years or 5.70% for two years from August 2023 instead of the tracker rate from March 2024.

I appreciate Mr A doesn't think that's fair. But I do think it's a fair way to resolve the complaint. It puts him back in the situation he would have been in September 2023 had Lloyds properly explained things to him – by giving him the choices now that he would have had then. I don't think it would be fair to remove all the interest above £453 added to the balance. That's because the only way the extra interest would never have been added was if Mr A had taken option one. But I don't think it's likely he would have done that.

Either option two or option three would have resulted in some increase to the balance, because Mr A wasn't paying any capital, and because the payments during the interest only period were set based on the lower fixed rate even though that expired in October 2023. So it wouldn't be fair to remove that now. What should happen is that Lloyds gives Mr A the choices he should have had at the time – and its offer does that.

## My final decision

My final decision is that Lloyds Bank PLC has made a fair and reasonable offer to settle this complaint. If Mr A now decides to accept that offer, it should implement the fixed rate he chooses with effect from 1 November 2023 – in place of the period on SVR and the tracker rate selected in March 2024. And it should re-calculate the mortgage balance and monthly payments on that basis.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr A to accept or reject my decision before 9 January 2025.

Simon Pugh
**Ombudsman**