

## **The complaint**

Mr M complains that Bank of Scotland plc trading as Birmingham Midshires (BM) failed to collect direct debits properly, leading to his mortgage going into arrears.

## **What happened**

Mr M had a residential mortgage with BM. He had been in a small amount of arrears dating from the coronavirus pandemic which he was paying off at £10 per month on top of his regular payment. In June 2022 he made a lump sum payment to clear the remaining arrears. At the same time, he asked BM to set up a direct debit to collect future payments (he had previously been paying by standing order).

One of the advantages of a direct debit is that it allows the bank to change the amount collected if the monthly payment changes – whereas the borrower would have to manually amend a standing order themselves. So Mr M thought that once the direct debit had been set up BM would then collect the right amount each month, and his mortgage would stay up to date.

Unfortunately BM set the direct debit up incorrectly on its systems. It set it up to collect a fixed payment, rather than – as is usual – a variable payment. This meant that when the Bank of England base rates started to increase – and so did the interest rate charged on Mr M's mortgage – the direct debit didn't change as it should have done and BM was no longer collecting enough each month to cover the monthly payment. The mortgage fell into arrears as a result.

At first, Mr M didn't realise this. BM did write to him about the arrears. But Mr M says that he didn't open its letters and blocked its calls and emails. He only realised the situation when he checked his credit file in February 2023 and saw the reports of arrears. He immediately contacted BM to correct the direct debit and clear the arrears.

Mr M complained to BM. It accepted that it had set up the direct debit wrongly. But it didn't agree to remove the record of the arrears from his credit file. It said that it had written to Mr M repeatedly to tell him about the arrears, and he ought to have acted on those letters. If he had done so, the situation would have been resolved much sooner. But it offered £50 compensation for the error in setting up the direct debit.

Mr M wasn't happy with that. He said that this situation had had a serious impact on him. BM wouldn't offer him a new interest rate and he was now unable to move his mortgage elsewhere. He wanted to move from his existing tracker rate to a fixed rate, but was unable to do so because of the arrears markers. He said he could have moved to a fixed rate of 3.89% with the Bank of Scotland brand. But he ended up having to sell his home because the mortgage was no longer affordable as interest rates increased – with his payments increasing from around £500 to almost £1,700 per month.

Mr M also said that during the period of arrears between 2020 and 2022, although the arrears amounted to only one month's payment and he was in an arrangement to clear them, BM kept writing to him and threatening legal action and repossession. He said that he

found these letters distressing as a vulnerable customer and asked BM to stop sending the letters but it wouldn't. So as a result, to protect his wellbeing, he threw letters from BM away without opening them. He also blocked its phone number so it couldn't call him. As a result, he didn't become aware of the error with the direct debit until he checked his credit file several months later. He said BM knew of his vulnerability and should take responsibility for the impact of its error.

I issued a provisional decision setting out my initial conclusions on the complaint and the further information I would need to determine it.

### **My first provisional decision**

I said:

"Although after 2020 Mr M was repaying the arrears, by June 2022 they were increasing again, because his mortgage was on a tracker rate and interest rates had risen, but Mr M hadn't changed his standing order. I can see that Mr M had made an earlier complaint about repeated contact, because he thought he was in an agreed arrangement to repay the arrears, but BM said there wasn't an arrangement and so it would need to contact him requesting information and chasing the arrears until there was. f

In a call with BM on 7 June 2022, Mr M agreed to pay off the outstanding arrears, and set up a direct debit.

Mr M says that BM was aware of his vulnerabilities – and I've seen that recorded in its contact notes. Mr M also says that on the 7 June call, he made clear to the person he spoke to that receiving letters and calls about the outstanding arrears had been distressing him, and that he no longer wanted contact. He says that one of the reasons he paid the arrears off immediately rather than continue gradual payments was so that the contact would stop.

Mr M says that he wanted to set up a direct debit for the same reason, and that he confirmed with the staff member that a direct debit would take the correct payment each month. As he was no longer in arrears he wouldn't receive regular letters about that, and BoS would only need to write to him when the interest rate changed (which he wouldn't need to worry about because the direct debit would adjust his payment) or with an annual statement. Mr M says that he confirmed this with the adviser he spoke to. While BoS had to continue to send those letters, he could safely ignore them.

We've asked BM to provide a copy of this call recording. But it hasn't been able to locate the recording, so I can't listen to it myself to confirm what was said.

I have reviewed the adviser's contemporaneous note. The note is relatively brief. It confirms that the reason the arrears were increasing was because Mr M hadn't adjusted his standing order. It records that Mr M paid off the arrears and requested a direct debit be set up. The note records that BM told Mr M that the direct debit would collect the June payment, due shortly, of £701.87. It records that Mr M was advised that BM would write to him confirming the direct debit had been set up. It also records that Mr M was advised he would be contacted again if there were further arrears and that arrears might impact his credit file. The call was then transferred to another member of staff to process Mr M's card payment clearing the arrears.

BM's note doesn't therefore record the part of the conversation Mr M says he had in which he was told that he could ignore future letters about payment changes and the annual statement.

However, that doesn't mean that I can disregard what Mr M says about this. It's clear from previous contact that he was vulnerable and found repeated contact from BM distressing. That corroborates his recollection that he tried to ensure that future contact either wouldn't happen, or wouldn't need his attention and could be ignored – as does his desire to move from a standing order to a direct debit. The absence of a record of this part of the discussion in the contact note doesn't mean it didn't happen – the note is a brief summary not a detailed transcript, and records an outline of the parts of the conversation the adviser thought important (which is not necessarily the same as the parts Mr M thought important). And the note is inaccurate in other respects – for example, the adviser recorded in the note that the direct debit had been set up to collect June's payment in full when it hadn't been, it had been set up at a fixed amount of around £480.

On balance, therefore, I accept Mr M's recollection of the conversation. I think he was upset at the repeated contact when he thought that an arrangement should be in place so contact wasn't necessary. He'd previously complained about that and when BM didn't agree he decided to clear the arrears and ensure they wouldn't be repeated – to stop the contact he found distressing. He checked that he'd done enough to ensure that, and could safely ignore future letters.

This is important context for what happened next. BM accepts that it made an error in setting up the direct debit, and that this was the cause of Mr M falling back into arrears. But it doesn't accept that it's responsible for the resulting impact on his credit file or any other consequences that may have flowed.

BM's argument here is that Mr M failed to mitigate his losses. Although it was at fault in creating the situation, it then did enough to put things right by repeatedly writing to Mr M telling him that his account was falling back into arrears. It took a few months before the amounts missed were enough to impact Mr M's credit file. If Mr M had read and acted on the letters BM sent, he would have contacted BM sooner and the mistake could have been corrected before that happened. So, BM says, while it made the mistake in the first place, the impact of it on Mr M is because Mr M unreasonably failed to take action when it told him there was a problem.

I've thought carefully about this. It's clear that none of this would have happened had BM not made the mistake in the first place. But – as a general principle – I also agree that there's a responsibility on borrowers to make sure they meet their obligation to pay their mortgage in full each month, and to pay attention to and act on important correspondence from their lender. Though that doesn't detract from a lender's obligation to get things right in the first place.

Mr M didn't read or act on the letters he received. He was caused loss by BM, and he didn't mitigate that loss when he had the opportunity to do so created by the letters from BM. But that's not enough; I also need to think about whether failing to do so was unreasonable in the particular circumstances of this case.

On balance, I'm not persuaded that Mr M acted unreasonably in his particular circumstances, or that his failure to act on BM's letters means that BM is no longer liable for the consequences of its mistake. Mr M was a vulnerable customer, and BM knew that. He'd taken particular action to make sure that his mortgage was brought back up to date and kept up to date in the future. He'd checked that his direct debit

would be varied when his payments changed, and while BM would need to write to him about payment changes he wouldn't need to take any action and could safely ignore those letters – given that he'd found the repeated correspondence from BM difficult and distressing.

In fact, BM did write to him repeatedly. But this was in the second half of 2022 and early 2023, when Bank of England base rate changed most months. Mr M was on a base rate tracker, so his interest rate and monthly payment would change every month too. Knowing that, Mr M would have expected to receive a letter telling him of that change, would have expected that his direct debit would automatically have changed, and would have understood that he didn't need to do anything and could safely ignore the letters. He'd specifically checked that he could do so in the June 2022 call.

So when the impact of BM's mistake began to be felt, and Mr M's direct debit payments fell short, BM wrote to him to tell him that. But Mr M had no way of knowing that was the case other than via the letters – and as he was expecting to receive letters that he didn't need to look at, he would have had no reason to look at these letters.

While Mr M might have noticed from his bank account that the amount being collected each month hadn't changed, the impact of base rate changes at this time was gradual, with relatively small changes each month. There would have been no reason for Mr M to actively compare one month's payment with the last, and so no reason he ought specifically to have questioned why BM wasn't collecting more from him – bearing in mind he'd been told to expect it to collect the right amount. He'd been given an assurance by his bank, and it's reasonable that he relied on it rather than second-guessing it, especially in circumstances where BM knew he was relying on that assurance to avoid his vulnerabilities being made worse.

I'm therefore satisfied that Mr M didn't act unreasonably in not opening and taking action on the letters BM sent to him. He would have had no reason to know that these were not routine letters notifying him of changes to his interest rate, that he could safely ignore. He would therefore have had no reason to contact BM or to have learned of the ongoing consequences of its mistake.

In the particular circumstances of this case, therefore, I don't agree with BM that Mr M unreasonably failed to mitigate his losses by not contacting BM when he received its letters. I'm satisfied that the ultimate failure here was BM's, and it's responsible for putting things right.

In order to do so, BM should remove the adverse entries from Mr M's credit file recorded as a result of this error. Mr M says that as a result of the problems with his credit file, he was unable to take a new fixed interest rate – with the result that his mortgage on the tracker rate became increasingly expensive and he felt forced to sell his property to avoid falling back into arrears.

I'm not persuaded it's likely that Mr M would have been able to move his mortgage to another lender, even without the problems BM caused with his credit file. I've seen that he had arrears recorded from the period before June 2022, which would still have been on his credit file even if BM had not made this mistake. I've also borne in mind that Mr M found increasing payments difficult to the point where he had to sell his property – which suggests that he would have struggled with a new lender's affordability assessment. I therefore think it's likely Mr M wouldn't have been able to take a new mortgage with a new lender even without the mistake BM made.

However, BM does allow customers to move internally – from the BM brand to the Bank of Scotland brand. Under the rules of mortgage regulation, that doesn't need an affordability assessment. Mr M believes that there was a fixed rate of around 3.89% available with Bank of Scotland that he could have moved to had his mortgage not been in arrears in early 2023.

I don't currently have enough information to be able to decide whether or not it's likely Mr M would have been able to move his mortgage from BM to Bank of Scotland but for this error. I therefore require Bank of Scotland to provide more information about its "internal re-mortgage process" so that I can decide this part of the complaint. I would also like Mr M to tell me more about his circumstances so that I can consider whether, if he could have taken a new rate with Bank of Scotland, that would have been sustainable for him. I will also need to consider whether selling his property was the only realistic option open to him when he wasn't able to take a new interest rate.

Once I've considered this, I'll be in a better position to assess the impact of BM's mistake on Mr M. If but for this error he would have been able to move to an affordable mortgage and wouldn't have needed to sell his property, the impact – and any compensation – is likely to have been greater than if he would never have been eligible to move in any case.

Once I have the information I need, I'll consider further what I think BM needs to do to compensate Mr M for what went wrong, and I'll let the parties have a chance to comment on my thinking before I make a final decision.

Bank of Scotland plc trading as Birmingham Midshires should provide me with the following by the deadline set out at the start of this provisional decision:

- Its full lending criteria for an internal re-mortgage from BM to Bank of Scotland in February 2023.
- Any reason why it believes Mr M may or may not have met those criteria at the time (had his mortgage not been in arrears and had all payments by direct debit since June 2022 been made as they should have been), together with a full explanation and evidence of why that is the case.
- The list of fixed rates available to customers with Mr M's then loan to value moving from BM to Bank of Scotland in February 2023."

### **The responses to my first provisional decision**

Both parties responded with further detailed information.

BM said that it had now managed to locate a recording of the crucial phone call, and apologised that it wasn't available sooner. It said that there was no discussion in the call about future arrears letters, but there was a discussion about the contractual monthly payment and how the direct debit would be automatically adjusted to collect the right amount. That is what should have happened – but unfortunately the call handler wrongly set the direct debit up as a fixed amount.

BM said that its process for allowing customers to move internally from BM to Bank of Scotland didn't require an affordability assessment where there was no change to the mortgage other than taking a new interest rate. But other changes – such as changes of

borrower, or applying for further borrowing, did require an affordability assessment. This is in line with what the rules of mortgage regulation require.

BM said that Mr M did make an application for a re-mortgage to Bank of Scotland in April 2023 – but this wasn't just an application for a new interest rate; he also wanted to remove the existing joint party from the mortgage and replace them with his current partner, and he wanted to apply for further borrowing. BM said that it considered that application but Mr M didn't meet its lending criteria – because he had an interest only mortgage with no repayment strategy (other than sale of the property), and because Bank of Scotland only offers new interest only lending (including further borrowing) to customers with income above a certain threshold and with equity in the property also above a particular threshold. Mr M's application didn't meet either of those criteria, so his application was also assessed to see whether switching to a repayment mortgage instead would be affordable – but it wasn't.

BM said that it also noted that the existing joint account holder hadn't agreed to a change of interest rate. And as Mr M and the joint account holder were trying to resolve ownership of this and another property it wouldn't be appropriate to apply a new fixed rate without their consent if they remained on the mortgage.

BM said that as a result of that it didn't think it had acted unfairly in declining Mr M's application. Although credit score had also been a factor in its decision – and credit score would have been affected by the problem with the arrears – it said that it believed applications to change borrowers and take further borrowing, and alternatively for a new interest rate without the other party's consent, would still have been declined even without the issue with the arrears.

Mr M also provided further detailed information about his situation. He said that he was currently working, but paying almost all his salary into his pension with a view to retiring in 2025. He said that when BM turned down his application he and his new partner applied elsewhere but were advised by a mortgage broker that the arrears would make a new application very difficult. In the end his new partner succeeded in obtaining a mortgage in her sole name – which left Mr M feeling he had no choice but to go ahead and transfer the property into her name, with obvious risks for his own future, and for his children's inheritance. She also had to pay legal and other fees, which wouldn't have been charged had the application been able to go ahead with BM.

## **My second provisional decision**

Having considered what both parties said, I issued a second provisional decision setting out my proposed outcome to the complaint. I said:

“Firstly, I'm very grateful to both parties for the very clear and detailed information they've provided in response to my first provisional decision. I now have all the information I need to reach an outcome to this complaint, and so I'm issuing this second provisional decision to explain what I think needs to be done.

While I am upholding this complaint, I am only doing so to a limited extent. I appreciate Mr M will be very disappointed with my conclusions, but I hope he'll understand my reasons for reaching them. And if Mr M – or indeed BM – has any further evidence or arguments for me to consider before making a final decision, I will of course give them very careful consideration.

It's very disappointing that BM was unable to locate the call sooner. However, now it has been located I've listened to it in full and it doesn't change my view of the case. I

now agree that, despite Mr M's recollection, there was no discussion of being able to disregard future letters. But Mr M was clear that he wanted a direct debit setting up so that his payments would be automatically adjusted to the right amount in future. That should have happened – and BM confirmed it would on the call – but it didn't, because the direct debit was set up wrongly. In the circumstances, it wasn't unreasonable for Mr M to have concluded that everything was, from then on, under control and so he didn't need to check future letters from BM. I say that bearing in mind his vulnerability at the time and the impact previous letters had had on him.

The key point here is that this was BM's mistake in not setting up the direct debit properly. That's why Mr M's mortgage fell back into arrears. And in the particular circumstances of this case, taking Mr M's own situation into account, I don't think it would be fair to say that he failed to mitigate his losses such that it wouldn't be fair to remove the markers from his credit file. Ultimately, those markers wouldn't have been there if BM had done what it was supposed to.

To that extent, my view of the complaint hasn't changed and I still think it should be upheld. In my first provisional decision, I wanted both parties to provide me with further information so I could decide whether further redress beyond correcting Mr M's credit file was appropriate.

This turns on whether it was purely the arrears resulting from the direct debit problem which prevented Mr M taking a new interest rate or a new mortgage with Bank of Scotland – or whether that application would always have been rejected even if the direct debit mistake hadn't happened.

On balance, I think it's more likely than not that Mr M's application would still have been refused even without the arrears markers. That's because he didn't just want a new interest rate, he also wanted to change borrowers and borrow more money. The existing mortgage was on interest only terms, but Mr M didn't have a suitable repayment strategy, and didn't qualify for a new, larger, interest only mortgage on income or loan to value grounds. So the only option would have been a repayment mortgage, which wasn't affordable.

I appreciate Mr M's partner was able to get a new mortgage in her own sole name with another lender. But I don't think that means that Bank of Scotland also would have lent to her and Mr M jointly without the arrears. The mortgage Mr M's partner arranged was very different – it was a repayment mortgage over a term of 36 years. A longer term makes a substantial difference to affordability of a repayment mortgage – the longer the term, the lower the payments – but given that Mr M is in his mid-fifties a mortgage over such a long term (ending at around age 90) wouldn't have been available to him with Bank of Scotland. A mortgage including Mr M would have to be over a much shorter term, which wasn't affordable on repayment terms.

That means that – regardless of the arrears markers – Mr M's application to replace this mortgage with a new, larger one in different names would always have been refused. He didn't qualify for an interest only mortgage and a repayment one wasn't affordable.

I'm also not persuaded that retaining essentially the same mortgage, but moving it to Bank of Scotland to obtain a new interest rate, would have been possible either. Mr M needed to remove his previous partner from the mortgage under the terms of the agreement between the two of them – which simply taking a new interest rate wouldn't have achieved. And to move to Bank of Scotland and take a new interest rate without removing her would require her to consent to the change. But she wasn't

party to this application and given that both she and Mr M wanted her removed from the mortgage, I don't think it's likely that's what Mr M would have wanted or that she would have consented. If a new interest rate was applied without her consent and the property ended up having to be sold or re-mortgaged because she couldn't be removed from the existing mortgage, there would be a substantial early repayment charge. It wouldn't be appropriate to take that risk without her consent.

Taking all that into account, I'm satisfied that the outcome would have been much the same even if BM's error hadn't led to the mortgage going back into arrears. Even without that, Mr M wouldn't have been able to make the changes to the mortgage that he wanted, and wouldn't have been able to take a new interest rate with Bank of Scotland. He and his new partner would have been faced with the same situation as they actually did end up in, and it's likely that the same outcome – with her taking out a new mortgage in her sole name – would have happened.

With that in mind, it wouldn't be fair to compensate Mr M for losing out on an interest rate he would never have got anyway, or the costs of moving the mortgage elsewhere that always would have been paid even without the arrears.

It's possible that without the arrears markers Mr M might have been able to be included on his new partner's new mortgage with the other lender, meaning he wouldn't have had to transfer the property to her. But on balance I don't think it's likely given what I've said about Mr M's age and the length of the mortgage term. I don't think that lender would have lent to Mr M over such a long term either – or that a much shorter term would have been affordable.

I'm therefore not persuaded that it would be fair to require BM to compensate Mr M for missing out on a new interest rate, or for the consequences of transferring the property to his partner so she could take out a sole mortgage to repay this one. I think it's likely both of those things would have happened anyway. But once BM has removed the arrears markers (as it will be required to do if my final decision is the same as this provisional decision and Mr M accepts it), there would be nothing to stop Mr M and his new partner applying to the new lender to add Mr M on to the mortgage, and putting the property into joint names, if doing so falls within its lending criteria.

However, I do think BM should compensate Mr M for the substantial trouble and upset the arrears markers caused him. It's clear he was very concerned about it and believed that it had had a very substantial financial impact on him – I've found that's not the case, but that doesn't change the fact that Mr M believed it did. In all the circumstances, I think £500 is fair compensation."

### **The responses to my second provisional decision**

BM said it had no further points to make. Mr M didn't agree with my second provisional decision. He said that an independent mortgage broker had confirmed that he and his new partner would have been able to obtain a mortgage but for the arrears resulting from BM's mistake – the earlier period of arrears wasn't an issue.

Mr M said that during the application for a new mortgage with BoS, he discussed the possibility of taking an interest only mortgage using property abroad as the repayment strategy, but decided to take a repayment mortgage. BoS agreed a decision in principle to lend the amount they needed over a term running to Mr M's 80th birthday. He said that his plan was to retire at around age 78. A repayment mortgage on those terms was affordable, and it was only rejected because of the credit file issue – BoS was only concerned with



“recent” mortgage arrears. The same happened when they applied to another lender; it was only the arrears caused by BM’s error that prevented Mr M being party to the new mortgage that ended up being taken out by his new partner alone.

### **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.

Mr M says that but for the error with the direct debit, he would have been able to take a new mortgage with BoS to replace the one with BM. But I’m not persuaded of that.

I’ve listened to the discussion he had with an adviser when he and his new partner applied for the BoS mortgage. The application failed on credit score – but the adviser also made clear that even if that had not been the case, BoS was only willing to lend a maximum of £61,000 over 16 years on repayment terms – which was much less than was needed to repay the BM mortgage, let alone provide the further borrowing they wanted.

I’m also not persuaded that it was only the direct debit error which led to the credit score fail. Even without that issue, Mr M had other missed or late payments recorded on his credit file, most recently in April 2022 when payment was made late, as well as other instances in 2021 and 2020. Those matters would still have been taken into account even if the direct debit error hadn’t occurred.

Having reviewed things again following his response to my second provisional decision, therefore, I’m still not persuaded that Mr M would have been able to obtain the mortgage he needed with BoS even without the direct debit issue. It’s likely the application would still have failed on credit score because of the earlier missed or late payments, and even if it didn’t BoS wasn’t prepared to lend the amount needed on affordability grounds.

For the same reasons, it’s likely Mr M would have had difficulty being party to the new mortgage with the new lender too. But, as I said in my second provisional decision, once BM has corrected his credit file there’s nothing to stop him applying to be added to that mortgage now. If that application is granted, that will put him back in the position he would have been in without the direct debit error. And if it’s refused, that will show that it wasn’t only the direct debit error that prevented him being party to it at the time.

I’m therefore satisfied that the outcome I proposed in my second provisional decision is a fair and reasonable way to resolve this complaint.

### **My final decision**

My final decision is that I uphold this complaint and direct Bank of Scotland plc trading as Birmingham Midshires to:

- Remove all adverse information reported to Mr M’s credit file as a result of the error in setting up the direct debit; and
- Pay Mr M £500 compensation.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr M to accept or reject my decision before 5 November 2024.

Simon Pugh  
**Ombudsman**