DRN-5138469

The complaint

Mr and Mrs G complain that Kensington Mortgage Company Limited hasn't applied overpayments to their mortgage correctly. They also complain that Kensington has unfairly prevented them from taking out a new interest rate on their mortgage, and hasn't provided them with any support.

What happened

Mr and Mrs G have an interest only mortgage with Kensington that was originally taken out with a different lender. The term of the mortgage is due to end in 2037. Over the years Mr and Mrs G have made overpayments each month in order to reduce the capital balance. In 2018 Mr and Mrs G contacted Kensington to ask what options and support were available to them as they were concerned they had an interest only mortgage and their property was in negative equity. Kensington said it was unable to extend the term of the mortgage, and Mr and Mrs G would need to seek independent advice about their situation.

Mr and Mrs G asked similar questions in 2021 and 2022. They also specifically asked about what interest rate products Kensington could offer to reduce their monthly payments. Kensington told Mr and Mrs G it wasn't able to offer any interest products and directed Mr and Mrs G to seek independent advice.

In 2023 Mr and Mrs G complained. They were worried they weren't going to be able to keep up with the increased monthly payments following interest rate rises, and were unhappy Kensington wasn't doing anything to help them. Kensington said it was unable to offer any alternative mortgage rates to Mr and Mrs G. It said it was only able to offer temporary assistance and for a longer term solution Mr and Mrs G would need to seek independent financial advice. It had agreed to discuss Mr and Mrs G's income and expenditure to see what support could be provided. It also said it could use the credit balance that Mr and Mrs G had accrued on the account towards reduced or suspended payments for a period.

Mr and Mrs G brought their complaint to our service. They were concerned that their overpayments hadn't been applied to their capital balance as they were sat on the account as credit, which Kensington had said they could use towards their monthly payments. Mr and Mrs G didn't want to have to use that money they'd intentionally overpaid to reduce the capital, they wanted Kensington to provide more meaningful, long-term support to ensure their mortgage would be repaid by the end of the term. They had spoken to financial advisers on several occasions about their situation and had been told that because of the negative equity in the property, their only option was to stay with Kensington.

Kensington said the mortgage was being serviced under the original terms and conditions of the account. It said when Mr and Mrs G asked for help in 2018, they were treated the same as all its other customers. For mortgages that didn't originate with Kensington, and for those whose reversion rate would have been higher on a new product than Mr and Mrs G were on currently, no new rates were available. It said the rates that were available in 2018 were for new customers and not existing customers.

My provisional decision

I issued a provisional decision in which I said:

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

<u>Mr and Mrs G's overpayments</u>

Firstly, I will address Mr and Mrs G's concerns about the way Kensington has applied their overpayments to the mortgage account. I understand they were surprised to hear they could use the 'credit' they'd built up on the account to offset future payments if necessary. They believed the overpayments had reduced their overall balance. Having looked at the way Kensington has applied the overpayments to the mortgage account, I'm not persuaded it has caused Mr and Mrs G a loss. That's because whilst it records the overpayment balance as a separate credit on the account, it still offsets the interest that's charged on the capital balance. So Mr and Mrs G aren't paying more interest than they should be.

<u>Mr and Mrs G's requests to switch to an interest rate product</u>

Mr and Mrs G have contacted Kensington in 2018, 2021, 2022 and 2023 asking for help and support. Whilst in 2018 they didn't specifically ask about interest rate products, I'm satisfied that based on the request Mr and Mrs G made, and that it was a general request for options and support, Kensington ought to have considered whether an interest rate product might have been appropriate in the circumstances.

Kensington has said that Mr and Mrs G weren't able to access a new rate because their mortgage didn't originate with Kensington, and the reversion rate they were paying was lower than the reversion rate would have been on any of their other products. Having considered what they've said, I'm not persuaded that was a fair and reasonable approach to take.

When considering whether Kensington has acted fairly, I need to consider the relevant rules, guidance, law and industry practice. The Financial Conduct Authority (FCA) has set out an evidential provision in the Mortgage Conduct of Business handbook (MCOB) in relation to the fair treatment of borrowers who are unable to 'shop around' and move their mortgage to another lender. I've set this out below, as I think it's relevant when deciding whether Kensington has treated Mr and Mrs G fairly.

MCOB 11.8.1 E says:

" Where a customer is unable to:

(1) enter into a new regulated mortgage contract or home purchase plan or vary the terms of an existing regulated mortgage contract or home purchase plan with the existing mortgage lender or home purchase provider; or

(2) enter into a new regulated mortgage contract or home purchase plan with a new mortgage lender or home purchase provider;

the existing mortgage lender or home purchase provider 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 (Customers' interests)."

Principle 6 says:

"A firm must pay due regard to the interests of its customers and treat them fairly."

I think this is relevant to Mr and Mrs G's complaint. I'll explain why.

Mr and Mrs G weren't able to vary their existing mortgage with Kensington. I'm also persuaded that they were unable to enter into a new mortgage contract with a new lender. Mr and Mrs G have said they had discussed their situation with a financial adviser and had been told there were no options available to them other than what Kensington could offer. Based on what I know about their mortgage and circumstances, I think that's likely. They had an interest only mortgage with no repayment strategy, and their property was in negative equity. Based on my knowledge of the industry at that time, the regulations that were in place to ensure lenders were lending responsibly, and what that meant for lending criteria across the market, I think Mr and Mrs G would have struggled to re-mortgage to another lender. So I think both sub-points (1) and (2) above apply.

Kensington wouldn't offer Mr and Mrs G an interest rate product because their mortgage did not originate with it. Whereas I'm aware that in 2018, Kensington did offer new interest rate products to existing customers whose mortgages had originated with it.

11.8.1 E does not require all customers to be treated the same. But it does, in my view, show that there may be unfairness where a borrower who is unable to move to another lender is treated less favourably than a borrower who shares similar characteristics, "for example, by offering less favourable interest rates or other terms". Where the lender offers less favourable interest rates to some customers, it may give rise to the possibility of unfair outcomes in some situations. 11.8.1 E suggests that the regulator considered there to be the potential for unfairness where borrowers are unable to shop around.

I've thought about whether Mr and Mrs G, whose mortgage was transferred to Kensington in 2016, could – at the time of the conversations in 2018, 2021, 2022 and 2023 - be considered as having similar characteristics as a different borrower with Kensington, who had taken out their mortgage with Kensington originally. I think this is the central question I need to decide. At the time of the conversations Mr and Mrs G had with Kensington, they had an interest only mortgage and were up to date with their payments (and had in fact overpaid). I think it's likely that there were other Kensington borrowers whose mortgages were in much the same position as Mr and Mrs G's mortgage at the time, and whose circumstances at that time would have been substantially similar. A significant amount of time had elapsed since 2007 when this mortgage was taken out, so I've considered whether the way in which the mortgage was originally taken out (i.e. with a different lender) can properly be said to be a 'characteristic' relevant to the risk Mr and Mrs G presented in 2018 and beyond.

I'm not persuaded that how the mortgage was initially taken out in 2007 was a relevant consideration or 'characteristic' in 2018. Mr and Mrs G had met the lender's eligibility and lending criteria as a new borrower in 2007. Kensington had agreed to take the mortgage on in 2016. But, as these criteria changed over time, following the introduction of tighter regulation and more stringent checks – Mr and Mrs G did not meet the new borrower criteria for other lenders by 2018.

I think it's likely that there were other Kensington borrowers who, although they'd passed Kensington's own lending criteria when the mortgage was taken out (whenever that was), would have been unable to pass the new, stricter lending criteria that existed in 2018. And just because they had taken their mortgage out with Kensington originally, doesn't mean they had the same circumstances relevant to the risk they presented in 2018, as they did at the point of origination. In fact, I think that's very unlikely. But they wouldn't have been prevented from accessing the cheaper rates. Mr and Mrs G have therefore been treated less favourably than Kensington's customers who took their mortgage out with Kensington originally. In my view, when considering 11.8.1 E, I think the characteristics of Mr and Mrs G's mortgage in 2018 are what's relevant.

When Mr and Mrs G asked about their options in 2018, I think Kensington ought to have looked into their situation, and considered whether or not MCOB 11.8.1 E might have been relevant, for example as here because they were unable to move to another lender. This doesn't appear to have happened. So I've gone on to think about what would have happened had Kensington considered Mr and Mrs G's circumstances fairly at the time.

Mr and Mrs G have said they were aware their property was in negative equity – that's one of the reasons they were asking Kensington for help in the first place. I'm aware that the interest rate products Kensington had available at the time were only available to borrowers who had a maximum loan to value of 90%. And whilst I think Kensington should have considered 11.8.1 E, and whether Mr and Mrs G were being treated less favourably than its other customers with similar characteristics, it is still entitled to have eligibility criteria for the products that it offers. And a customer who had a mortgage that had originated with Kensington, and whose property was in negative equity, wouldn't have been eligible for a new rate either. So I'm persuaded that even if Kensington had fairly considered Mr and Mrs G's requests at the relevant times, I don't think they would have been able to take out a new interest rate product based on the loan to value of the property.

It's also worth noting that Mr and Mrs G's mortgage is on a variable rate that has tracked Barclays bank base rate, which in practice is the same as Bank of England base rate. That meant in 2018 their interest rate was 2.89%, and the products Kensington was offering at the time had higher rates than that. So overall, whilst I don't think Kensington considered Mr and Mrs G's requests fairly – I don't think Mr and Mrs G have lost out as a result.

I understand Mr and Mrs G still feel their property is in negative equity (and has been for many years), but it's not clear whether they've had a recent valuation done to confirm that. If Kensington has any interest rate products available to its customers that are lower than the rate Mr and Mrs G are currently paying, and Mr and Mrs G would still like to apply for a new rate with Kensington, I'm satisfied Kensington should fairly consider an application, taking into account and applying the considerations I've set out in this decision. If, after a valuation is completed, it is found the property isn't in negative equity and Mr and Mrs G meet the eligibility criteria – including loan to value - for the product they have selected (disregarding when and how their mortgage originated), then Kensington should make that product available to Mr and Mrs G.

<u>The support Kensington has offered Mr and Mrs G</u>

Mr and Mrs G asked Kensington about lower interest rate products over the years, which I've addressed above, but they also asked about other support and options that Kensington could help with to ensure their mortgage was repaid by the end of the term.

Until 2023, when Kensington offered to discuss Mr and Mrs G's circumstances and go through an income and expenditure assessment, it had told Mr and Mrs G that it couldn't help them and directed them to seek independent financial advice.

Mr and Mrs G weren't in financial difficulties when they contacted Kensington and asked for help with their mortgage. They were being proactive and trying to address the long term issue they were aware they had which was their mortgage was interest only and they had no way of paying it back at the end of the term. They were concerned that selling their property wouldn't even repay the capital. I'm persuaded that as a responsible lender, taking account of the regulator's principles, Kensington ought to have engaged with Mr and Mrs G's requests and considered whether there was anything it could do to help rather than just direct them to seek independent advice. Kensington is required to treat its customers fairly and has particular obligations to assist interest only borrowers at risk of not being able to repay the mortgage capital, and so I think it ought to have reviewed Mr and Mrs G's circumstances at the time to see what could have been available.

Mr and Mrs G were already overpaying on their mortgage each month. They weren't making lump sum overpayments, but were paying more than their contractual monthly payment and so gradually built up a credit balance on the account. In terms of long term support or changes that Kensington could have made to the mortgage, considering the circumstances I think the options it reasonably ought to have considered were either to switch the mortgage to repayment, or extend the term, or a combination of the two.

In 2018 Mr and Mrs G's mortgage balance was around £231,000 and they had 19 years left on the existing term. Switching the mortgage to repayment would have significantly increased the monthly mortgage payments to more than double what they were at the time. Based on the fact Mr and Mrs G were aware of their situation and were trying to mitigate the issue by making overpayments, I think if they could have afforded to pay more towards the mortgage then it's likely they would have.

Extending the mortgage term on an interest only basis as it was wouldn't have resolved Mr and Mrs G's problem at the time. There were still 19 years left on the term, and Mr and Mrs G's circumstances could have changed significantly during that time. It's not clear there would have been any benefit to extending the term on an interest only basis. However, Kensington could have considered extending the term and switching the mortgage to repayment to try and establish whether that would have made the monthly payments affordable for Mr and Mrs G. But again, based on the small amount of overpayments they were making each month, I'm not currently persuaded there would have been a way to do this that would make the mortgage payments affordable, keeping the term within a reasonable period considering Mr and Mrs G's retirement plans etc. As the mortgage term as it currently stands already runs until Mr G is 61. But if Mr and Mrs G think I'm wrong about that, then I invite them to provide further submissions in response to this decision.

I'm pleased to see Kensington did discuss forbearance with Mr and Mrs G when they contacted it in 2023 about their concerns resulting from the increasing monthly payments.

<u>Summary</u>

Overall, whilst I'm satisfied Kensington has not treated Mr and Mrs G fairly when they've requested help and support, I'm not currently persuaded they've experienced a financial loss as a result.

As Mr and Mrs G are unable to re-mortgage elsewhere, I do think they need to have a conversation with Kensington about what long term options might be available to help them repay this mortgage. Kensington should engage meaningfully in those discussions, and be open minded about what it might be able to do to help based on Mr and Mrs G's circumstances, and its obligations to treat them fairly and reasonably. This includes, but is not limited to, looking at the interest rate, the repayment method, and the mortgage term.

I am persuaded Kensington has provided Mr and Mrs G with poor customer service over the years and has failed to engage with their requests for help. I think this has caused Mr and Mrs G distress, inconvenience, and increased worry about their financial situation. As a result, Kensington should pay Mr and Mrs G £250 to reflect the distress it has caused them."

Responses to my provisional decision

Both parties responded and explained they didn't have any further comments to make.

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.

As neither party has provided any comments in response to my provisional decision, I see no reason to depart from the findings I made, and outcome reached. I adopt the reasoning set out in my provisional decision in this final decision.

Putting things right

For the reasons I explained in my provisional decision, Kensington Mortgage Company Limited must pay Mr and Mrs G £250 for the distress and inconvenience caused.

My final decision

I uphold this complaint in part, and instruct Kensington Mortgage Company Limited to put things right as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs G and Mr G to accept or reject my decision before 9 December 2024.

Kathryn Billings
Ombudsman