complaint

Mr and Mrs K are unhappy Santander UK Plc didn't let them extend the term of their mortgage. And that it withdrew their flexible reserve fund facility.

background

I'll start by setting out the factual background to this complaint. And then reminding the parties what I said in my provisional decision. I'll then explain the final decision I've made.

circumstances

Mr and Mrs K took the mortgage out in 2003. It was taken out with their late father as he was exercising his right to buy option on the property. The mortgage was on a capital repayment basis. It was a flexible mortgage which included a 'reserve account' giving Mr and Mrs K the ability to withdraw extra funds from the account; subject to a certain limit.

Between July and August 2014, Mr and Mrs K got in touch with Santander. At that time the mortgage had about 8 years left. They asked to extend the term so there'd be 15 years left to run. When making the application, they said Mr K's income had recently reduced and Mrs K wasn't working as she was looking after their newly born son. Extending the term would make the mortgage more affordable going forward; halving their monthly repayments. A 15 year extension would mean the mortgage was due to finish when Mr K (the older of the couple) was in his early 60s.

Santander declined the request and a further request that Mr and Mrs K made in September 2015. It said the proposed mortgage wasn't affordable.

A few weeks later Santander withdrew the reserve account facility on the mortgage. It sent a short letter to Mr and Mrs K on 9 November 2015 saying that as they'd been using the facility to fund their mortgage repayments, they'd have to find an alternative way to meet the payment due on 3 December 2015.

Mr and Mrs K said they had to rely on the reserve account because Santander refused to extend the term of the mortgage. They've also had to borrow from friends and family and use credit cards and overdrafts. All of which has made their financial situation worse. Despite this, they say they've made every mortgage repayment on time since 2003. And point out that they have a large amount of equity in the family home as well as buy-to-let properties.

my provisional findings

I sent both parties my provisional decision on 4 November 2016.

Briefly, I said that based on the evidence so far I intended to uphold the complaint. I said I didn't think Santander had treated Mr and Mrs K fairly or acted in their best interests when it declined their request to extend the mortgage term. I also said that I didn't think Santander had treated Mr and Mrs K fairly by withdrawing the reserve account facility in the way that it did.

In that provisional decision, I set out how I thought Santander should put this right. That involved extending the mortgage term, adjusting the outstanding balance and calculating the 'overpayments' Mr and Mrs K have made and adding interest to those 'overpayments'. I said

I thought interest should be at 8% simple per annum which represented a fair and pragmatic figure to balance out the times Mr and Mrs K borrowed at rates higher and lower than 8%. I asked Mr and Mrs K to let me know whether they wanted the 'overpayments' paid directly to them or used to reduce the outstanding mortgage balance. I also asked Santander to reinstate the reserve account. And pay £500 for the distress it caused by not dealing with their term extension request fairly and for the way it withdrew the reserve account.

I invited both parties to make any final points they wished me to consider before I reached my final decision. Both parties responded to my provisional decision. I've considered those responses in full. But I've only included a summary of them below.

Mr and Mrs K say there are some issues with my proposals to deal with their financial loss. And what I've described as 'distress' in my provisional decision. Briefly, they say:

- It's not fair for the interest on the 'overpayments' to also cover other financial losses. They have identified other funds they received and were offered to help them which they think should be paid to them too. As well as a number of other fees, charges and interest which they say have directly resulted from Santander's actions.
- That the £500 I proposed for 'distress' is insufficient. And that based on the guidance on our website, their complaint falls into the 'higher end of severe' category so warrants a payment of between £2,000 and £5,000.
- That I didn't consider other elements of compensation such as for their pain and suffering. They both have health issues which have been made worse by this complaint and for which I said I didn't need documentary evidence. They've experienced reduced living standards for 2 years causing considerable distress and embarrassment. They say this means they've had to cut back on essentials like clothing and heating for their children in order to keep up repayments and this has had an impact on their children's emotional wellbeing.
- That they've spent 100s of hours dealing with these issues and should be compensated for their time.

Santander still thinks the complaint should be declined. Briefly, it has said:

- When Mr and Mrs K got in touch in 2014 about the term extension, Santander was made aware that Mr K's income had reduced and Mrs K was no longer working as she was looking after their young family. Santander refused the request on grounds of affordability and its approach was to assess whether they could afford current repayments and repayments in the future if interest rates were to rise. It points out that such rises would directly affect Mr and Mrs K as they have a mortgage which tracks the Bank of England base rate. It also undertook an affordability assessment to establish whether the request was due to financial difficulty. It says if it wasn't, it could potentially have agreed to the request. But if it was, it would apply its forbearance solutions and strategies through its collections and recoveries department. Only in February 2016 were Mr and Mrs K prepared to talk to that area of its business.
- It says it was allowed to ignore the affordability assessment set out in MCOB 11.6.2 where - amongst other things - there were no changes likely to be material to affordability. But Mr and Mrs K made them aware of a drop in income so the new circumstances *were* a material change. Indeed, Mr and Mrs K had made it clear the existing mortgage was no longer affordable and was being partly funded by the reserve account.

- The initial borrowing and additional borrowing facility were agreed based on the income of the original 3 parties to the mortgage. It's not unreasonable for Santander to expect to be informed of any significant changes to circumstances. Santander was told in September 2015 that the late Mr K had passed away in 2006 and this represented a material change as outlined in MCOB 11.6.4.
- The term extension would reduce the monthly repayments but would still result in an affordability deficit. Agreeing to a term extension which results in an unaffordable mortgage payment isn't appropriate forbearance action and isn't in the customer's best interests. Allowing such a change would go against good practice.
- Mr and Mrs K have provided conflicting information about their income/outgoings but an independent charity has suggested they make use of their available assets to pay off their debts. And the equity in their rental properties is significant and could be used to raise funds to reduce or repay their residential mortgage.
- It's acted fairly and extending the mortgage term would not be in Mr and Mrs K's best interests.
- The drawdown facility is not designed to be used to meet mortgage repayments. As soon as this came to light it indicated the consumer's position had changed and it was removed in line with the condition which states: *"we reasonably think that, because of a change in your financial position, you could not afford to repay present or future drawdowns up to the existing credit limit"*. In order for it to be reinstated, it's not unreasonable for Santander to ask for income and expenditure details. And it would likely have been reduced earlier if Santander had been made aware of the death of the late Mr K. Since his death in 2006, the funds drawn from the account substantially exceed the repayments made. And in the early part of 2014 - prior to the extension request - large withdrawals were made suggesting financial difficulties at that point.

my findings

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint. In deciding what's fair and reasonable, I've taken into account the relevant regulatory rules and guidance as well as the law and good industry practice at the time.

Overall, I've reached the same conclusions as the ones set out in my provisional decision.

the term extension

Santander provided a detailed response to my provisional decision setting out why it thinks it acted fairly - and in Mr and Mrs K's best interests - by turning down their request for an extension to the mortgage term. But it hasn't raised any new points. Having thought again about everything it's said, I still think it didn't treat Mr and Mrs K fairly or act reasonably or in their best interests by turning down the extension request.

As I explained in my provisional decision, since Mr and Mrs K first took their mortgage out, the rules on mortgage lending have been tightened. The industry regulator recognised this might cause difficulties for some people with existing mortgages who wanted to make changes to those mortgages. So it introduced flexibility into its rules to help lenders treat those existing borrowers fairly. That flexibility included giving lenders the ability to waive some of the new rules for existing customers. And also meant some of the requirements didn't actually apply to existing customers in certain circumstances.

Santander turned down Mr and Mrs K's request for a term extension saying it wasn't affordable. But the requirement for an affordability assessment was one of the rules which didn't apply in certain circumstances or which Santander was allowed to waive (through either MCOB 11.6.3 or 11.7.1). The requirement for an assessment didn't apply where an existing customer was making an application which didn't involve additional borrowing and didn't involve a change which was material to affordability (MCOB 11.6.3). If the change was material to affordability, it could waive the affordability assessment if the transaction was in the best interests of the customer (MCOB 11.7.1). It could do this if there hadn't been a further advance to the borrowing limit after 26 April 2014 (and there hadn't in Mr and Mrs K's case and they had kept within the agreed limit). The rules also allowed Santander to waive the affordability assessment where a variation was being made to avoid a payment shortfall. More generally, the rules required Santander to treat Mr and Mrs K fairly and to act in their best interests.

Mr and Mrs K's application didn't involve additional borrowing. And I said in my provisional decision that I didn't think Mr and Mrs K's application involved a change material to affordability. The rules give examples of what the regulator considers to be a change material to affordability (MCOB 11.6.4). One of those examples is extending the mortgage term into retirement and although Mr and Mrs K were proposing to extend the term, the new term wouldn't run past Mr K's expected retirement. But Santander says it thinks there was a material change to affordability because Mr and Mrs K told it that Mr K's income had dropped and that Mrs K had paused working to look after their young child. And that the late Mr K was being removed from the mortgage which is an example of a material change given under MCOB 11.6.4.

I don't agree with Santander that the change in income represented a material change of the sort referred to in MCOB 11.6.3. Although Mr and Mrs K's circumstances had changed (which is not unusual during the lengthy period a mortgage usually runs for) the rules say the question is whether there's a proposed change to the *terms of the mortgage* likely to be material to affordability. And the change in income Santander refers to is not a change to the terms of the mortgage. Having said that, I agree with Santander that the removal of a borrower is something the regulator says would be material to affordability. But the late Mr K died 8 years before this application was made. Although it's not clear to me where fault lies for not removing him from the mortgage earlier, that was a separate request to the application for a term extension and Santander agreed to do it as it was clearly in the best interests of the remaining parties for this to happen.

Having said all that, if I'm wrong and there was a material change to affordability this simply means that MCOB 11.7.1 rather than MCOB 11.6.3 could've been used by Santander to waive the requirement to do an affordability assessment. The main difference between the two rules which is relevant to this case is that MCOB 11.7.1 specifically says the transaction needs to be in the consumer's best interests. This is something I'd considered anyway as the rules more generally require Santander to act in Mr and Mrs K's best interests. So even if there was a material change to affordability it doesn't change my conclusion that Santander didn't need to complete an affordability assessment.

I have to now consider whether Santander treated Mr and Mrs K fairly and acted reasonably and in their best interests by conducting an affordability assessment when it didn't need to and then using the results of that assessment to turn down their application.

Mr and Mrs K recognised they were beginning to have difficulty meeting their monthly mortgage repayments as a result of Mr K's income falling and Mrs K being at home to look after their newly born son. Rather than waiting for things to deteriorate, Mr and Mrs K took the sensible step of putting forward their own solution to these difficulties by proposing to increase the mortgage term which would halve their monthly repayments (reducing them by roughly £1,000 each month). Clearly this would make the monthly mortgage repayments much more affordable for Mr and Mrs K.

Santander said it wouldn't agree to the proposal as it didn't think the lower repayment amount was affordable. It didn't seem to recognise at the time the request was first made that it was not required to complete (or could waive) the affordability assessment under the rules. It didn't offer Mr and Mrs K an alternative or appreciate that by turning the request down it was leaving them in a situation where they had a significantly more unaffordable mortgage. Whether or not it would continue to leave them with an unaffordable mortgage is subjective and there is conflicting evidence. It's also more difficult to determine this with any certainty given there would be such a large reduction in the monthly repayments. However, I'm not persuaded the proposal was unaffordable based on the evidence I've seen. In any event, overall, I don't think Santander's approach was reasonable and I don't think it treated Mr and Mrs K fairly here. One of the reasons the regulator included flexibility in the rules for existing borrowers was to help lenders avoid situations where they were turning down applications under strict affordability assessments when what was being proposed was actually more affordable than what the consumer currently had and made the mortgage much more manageable.

Santander continues to say Mr and Mrs K could instead have used some equity in their buy-to-let properties to reduce this residential mortgage or perhaps sell those properties to repay the mortgage. That's true. Although it wasn't something Santander suggested at the time. If it had explored this with Mr and Mrs K it would've been clear that this option was out of the question for them. And I think if Santander had put its mind to this it would've realised why. Any equity released from the buy-to-let properties will likely incur interest at a much higher rate than the 0.75% above the Bank of England base rate that they secured with Santander when they first took the mortgage out in 2003. Which would increase their regular outgoings. And if they sold those properties instead, they'd lose the income they provide.

The actual proposal Mr and Mrs K made was reasonable and still in their best interests. From Santander's point of view, I think it had its advantages as it meant Mr and Mrs K would have a much better chance of keeping up with their repayments without Santander needing to explore forbearance solutions. And it didn't involve the more significant changes to the risk it was exposed to which might've come with something like additional borrowing. It didn't involve extending the term into retirement either. It was simply a request to extend the term of the mortgage for a few years in order to make things a bit more manageable.

My role as an ombudsman is to look at Mr and Mrs K's complaint and to decide it by what I consider to be fair and reasonable in all the circumstances. I've looked at and taken into account the relevant regulatory rules and guidance. But I've also thought about whether in a wider sense Santander treated Mr and Mrs K fairly. Overall, I've concluded that Santander didn't treat Mr and Mrs K fairly or act reasonably or in their best interests by refusing their request to extend the mortgage term.

the reserve account

I've thought very carefully about the further points Santander made about this as I said in my provisional decision that there might be fair and legitimate reasons for Santander's actions.

But Santander still hasn't persuaded me it acted reasonably or treated Mr and Mrs K fairly by withdrawing the reserve account facility in the way that it did.

As I explained in my provisional decision, Santander knew Mr and Mrs K were using the facility to maintain their mortgage repayments while this dispute was ongoing. Despite that, it sent a short letter saying the facility was being withdrawn and that they needed to find another way to meet their next mortgage payment which was due in less than a month. It should've been clear to Santander that this would likely make Mr and Mrs K's financial situation worse and that it wasn't giving them much time to sort an alternative out.

The explanations Santander has so far given for its actions continue to be limited and don't persuade me that it's acted reasonably or treated Mr and Mrs K fairly.

Santander say Mr and Mrs K were using the reserve account to meet mortgage repayments and have referred to some large lump sum withdrawals which were made in the early part of 2014 (before Mr and Mrs K made the original term extension request). But as I said in my provisional decision, some of their behaviour in the later part of 2014 onwards resulted from Santander turning down a term extension request I think it should reasonable have approved. And the flexible mortgage account terms and conditions don't prevent usage like this. It also seems to me that making lump sum withdrawals was one of the behaviours that the reserve account was specifically designed for. It's not necessarily an indicator of financial difficulty. It seems to me that the lump sum withdrawals made before 2014 were likely to be Mr and Mrs K using the reserve facility to borrow lump sums at a much lower rate than they'd have otherwise been able to on the open market. Given that the tracker deal Mr and Mrs K took out in 2003 has become more and more competitive as interest rates have fallen.

In response to my provisional decision Santander has cited concerns about Mr and Mrs K's ability to repay the drawdowns and referred to the mortgage condition which says: *"we reasonably think that, because of a change in your financial position, you could not afford to repay present or future drawdowns up to the existing credit limit"*. I acknowledge the existence of that condition. But Santander still needs to rely on it fairly and I don't think it has. I say this because Santander acknowledges Mr and Mrs K have significant assets elsewhere and could use those assets to repay the reserve account borrowing at any time they wished. So I don't think Santander has any reasonably founded concerns about Mr and Mrs K being unable to repay this borrowing in the longer term. The difficulty Mr and Mrs K currently have is one of meeting their regular monthly repayments. And it's a difficulty which the term extension will go a long way to alleviating. This doesn't mean Santander *can't* make changes to the reserve account in the future. It just means that I don't think it treated Mr and Mrs K fairly and reasonably by withdrawing it in these circumstances and by giving such little notice.

I've also thought again about the late Mr K. Because Santander says the death of a borrower with an income would normally lead it to consider whether the remaining borrowers could afford to repay it. But as I said in my provisional decision, when the mortgage was taken out, Mr K's father was approaching 78 years of age and it's unlikely his retirement income played a significant part in the original lending decision. Mr and Mrs K have also maintained mortgage repayments for many years without him and - as I said above - Santander knows Mr and Mrs K have significant assets elsewhere.

Overall, I've concluded that Santander didn't act reasonably or treat Mr and Mrs K fairly by withdrawing the reserve account in the way that it did. But this decision doesn't prevent Santander from making changes to Mr and Mrs K's reserve facility in the future. However, if it decides to do so it should remember to apply its terms and conditions in a fair and reasonable way.

fair compensation

I continue to think that the steps I set out in my provisional decision for Santander to take to put matters right represent fair compensation in the particular circumstances.

However, I'll now explain why the two areas Mr and Mrs K disagreed with haven't led to me making changes to my award.

Mr and Mrs K made comments about how I'd assessed their financial loss. However, I think some of those comments have resulted from a misunderstanding of what I was proposing. Mr and Mrs K seem to think that I was saying interest should be paid *instead* of Santander refunding what they borrowed to meet the element of their mortgage payments which they wouldn't have been paying if the term extension had been granted. But the steps I said Santander should take included it adjusting the outstanding mortgage balance and refunding the overpayments (with interest). This means any money Mr and Mrs K borrowed to meet the higher mortgage repayments will be returned to them through the return of the 'overpayments'. The pragmatic approach I referred to was simply in relation to the use of an interest rate of 8% simple per annum on the 'overpayments'. This approach is because of the practical difficulties there will be in establishing the source (or sources) of funds for each individual mortgage payment and because some of the money they borrowed will have incurred interest at less than that (perhaps that from friends and family) and other money will have been more than that - such as loan or credit card - and might've resulted in some associated charges. I think such an approach is fair and reasonable in the particular circumstances.

The second area of disagreement is the award I said I intended to make to cover the non-financial loss. Mr and Mrs K are right to say that where I uphold a complaint, my powers allow me to make awards for pain and suffering, damage to reputation and distress or inconvenience. I also accept what Mr and Mrs K say about the impact this matter has had on them and their family. Which is why I haven't asked for medical evidence to support what they say. And I acknowledge they've spent a lot of time dealing with this complaint.

I also acknowledge we give examples on our website of situations where we might award more than I've currently proposed. But there's also examples of situations where we've awarded less even though what's happened has had a considerable impact on the consumer. And these examples are only guidelines designed - at least in part - to show that the circumstances of each complaint are different. As is the impact on the individual people involved.

I've thought about this matter very carefully. But I still think that the £500 I originally proposed for non-financial loss is fair and reasonable in the particular circumstances. And properly reflects the substantial impact - particularly the distress - I think this has had on Mr and Mrs K and their family.

my final decision

It's my final decision to uphold this complaint and order Santander UK Plc to do the following:

- Extend the term of Mr and Mrs K's mortgage on the basis that the original 2014 request for it to be extended so 15 years remained should've been accepted. And that this would've been implemented a few weeks later; I think a date of 1 October 2014 is reasonable.

- Calculate the 'overpayments' Mr and Mrs K have made since 1 October 2014. By 'overpayments' I mean the slice of the monthly repayments Mr and Mrs K have been making which they wouldn't have needed to make if the term had been extended (and therefore the repayments reduced) on 1 October 2014.

- Return those 'overpayments' and add interest to them from the date Mr and Mrs K made them to the date this money is returned. Interest should be at 8% simple per annum. I think this is a fair and pragmatic figure that attempts to balance out times Mr and Mrs K used the reserve account and friends and family to help with the mortgage payments with times they used more expensive borrowing such as credit cards and overdrafts. If Mr and Mrs K decide to use some or all of this money to reduce the mortgage Santander should allow them to do this (without imposing any sort of cost) within 1 calendar month of it making payment to them in settlement of this complaint.

- Adjust the outstanding mortgage balance on the basis that it would currently be different if Mr and Mrs K had extended the term of the mortgage on 1 October 2014 and had been making lower repayments since then.

- Pay Mr and Mrs K £500 for the distress it caused by not dealing with their term request extensions fairly and for the way it withdrew the reserve account.

- Reinstate the reserve account.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr and Mrs K to accept or reject my decision before 13 February 2017.

Graham Booth
ombudsman