

The complaint

Mr and Mrs M's complaint follows an ombudsman's decision dated 10 February 2022. Mr and Mrs M say that National Westminster Bank Plc (NatWest) failed to follow the ombudsman's direction to switch their mortgage onto an interest-only basis. They consider it unfair that NatWest treated this as an application that needed an affordability assessment, and that it was therefore unfair for the underwriters to have declined the application on the basis of mortgage arrears.

Mr and Mrs M say that the mortgage arrears (currently around £190,000) are "*a technicality*" because they've considered their mortgage to be interest-only since 2019, and so are up-to-date with the interest payments.

To settle the complaint, Mr and Mrs M want NatWest to engage with them in a "*meaningful*" way regarding their switch to an interest-only mortgage, and to compensate them for the additional interest they have been charged by being on the bank's Standard Variable Rate (SVR).

What happened

I do not need to set out the full background to the complaint. This is because the history of the matter is set out in the correspondence between the parties and our service, so there is no need for me to repeat the details here. In addition, our decisions are published, so it's important I don't include any information that might lead to Mr and Mrs M being identified. So for these reasons, I will instead provide a brief summary and then concentrate on giving the reasons for my decision. If I don't mention something, it won't be because I've ignored it; rather, it'll be because I didn't think it was material to the outcome of the complaint.

Mr and Mrs M have a capital repayment mortgage with NatWest. Since late 2019 they have been making payments of only the interest, as they consider their mortgage should be conducted on an interest-only basis, not capital repayment. As a result, substantial arrears have accrued.

On 10 February 2022 an ombudsman issued a final decision on a complaint raised by Mr and Mrs M. The complaint was that, during a period of financial difficulty, NatWest had failed to treat them fairly by not switching their mortgage onto an interest-only basis.

In his final decision the ombudsman found that in October 2019 NatWest had agreed to accept reduced payments to the mortgage for a couple of months.

The ombudsman also said:

I've thought about whether NatWest acted unreasonably by not switching the mortgage to an interest only basis once this was mentioned in February 2020. There seems to have been some miscommunication over how an application would need to be made, with the relationship managers at NatWest saying Mr and Mrs M needed to contact a mortgage adviser. But Mr and Mrs M said they were referred

back to the relationship managers. This breakdown in communication is unfortunate. But ultimately, I can't see that a formal application was made for this change to the mortgage to take place.

NatWest has said that changing the mortgage to an interest only basis would've involved a new mortgage application and a full assessment of the circumstances, including affordability and the intended repayment vehicle. I think this is reasonable. And I don't think were any grounds, in the circumstances of this request, on which NatWest ought to have set aside its usual lending criteria.

Mr and Mrs M have said they think they meet the criteria NatWest set out on its website about interest only mortgages. And they've continued to make payments equivalent to those required on an interest only basis since the dispute began. So, they believe the switch should've been made. But I don't agree.

As I've said, I think it is reasonable that NatWest would undertake a full mortgage assessment – something that has not happened. And things NatWest would've needed to consider when looking at an application would not solely be limited to the outline conditions on its website. These were likely to include whether the mortgage was up to date – which it wasn't – and plans for addressing this – which there weren't at the time with the previous arrangement having been broken. As well as an assessment of the plan to repay the mortgage and whether this was acceptable.

While Mr and Mrs M have said they think they meet the criteria, as I've mentioned, despite several requests by NatWest for evidence to support things Mr and Mrs M have said about their finances, information has not been forthcoming. I acknowledge Mr and Mrs M have been making payments – albeit without the change having been agreed. But NatWest has to ensure it acts responsibly. And making payments to the mortgage doesn't mean that it is affordable to do so over the longer term or that Mr and Mrs M would satisfy all of NatWest's criteria around affordability.

So, I don't think NatWest has acted unreasonably by not switching the mortgage to an interest only basis. I don't think it needed to do this without a proper assessment. And it hasn't been given the opportunity to carry one out.

Mr and Mrs M have paid less than the contractual monthly repayments since March 2020. I understand they've done this as they've said they wanted to switch the mortgage to an interest only basis, so have paid an equivalent amount. But that change has not been agreed. So, the payments were less than contractually required. As a result, I think NatWest acted fairly by recording information with credit reference agencies to reflect this.

Mr and Mrs M have also said that their interest rate has increased, as a result of their previous interest rate deal ending. But I haven't seen anything that leads me to think the increase was not in line with the mortgage agreement.

Taking everything into account, I don't think NatWest has acted unfairly or unreasonably in how it has handled Mr and Mrs M's accounts.

Moving forward, I understand there is now a significant arrears balance on the mortgage. And NatWest is considering further recovery action, via the courts. I would remind NatWest that possession proceedings should be a last resort. I can understand why it thinks there is now no alternative. As there has been little engagement for over a year and the arrears balance is now significant.

I do think though at least some of the deterioration in the overall position has been due to both parties awaiting the outcome of this complaint. Before proceeding with legal action, I'd expect NatWest to contact Mr and Mrs M, to see if there any remaining alternative options now available. I appreciate these may be limited. But I think they should be explored. I'd add though that, Mr and Mrs M would also need to engage with NatWest and importantly provide evidence, when requested, to support any suggested plans. And if this is not forthcoming, I think NatWest would fairly be entitled to decide how to pursue the matter further.

What has happened since the ombudsman's decision on 10 February 2022 is that an application was made by Mr and Mrs M for their mortgage to be switched to interest-only. However, after underwriters considered the application it was declined, not just because of the substantial arrears on the mortgage (and for which Mr and Mrs M had no repayment strategy), but because of other adverse credit information. The application therefore didn't meet NatWest's lending criteria and the bank declined it.

Mr and Mrs M raised another complaint, because they think NatWest has treated them unfairly. Mr and Mrs M said that they have attempted to engage with NatWest about the mortgage since the previous ombudsman's decision. Mr and Mrs M said they've paid interest in accordance with NatWest's interest-only product since March 2020, and have been forced to be on SVR. Mr and Mrs M considered NatWest had failed to act in accordance with Financial Conduct Authority (FCA) guidelines to treat them fairly or give them a reasonable timescale to repay the mortgage.

An investigator looked at what had happened but didn't think the complaint should be upheld. He was satisfied that NatWest had given fair consideration to the application to switch the mortgage to interest-only, and that the bank was entitled to decline the request.

Mr and Mrs M asked for an ombudsman to review the investigator's findings. They've reiterated some further points, which I summarise below:

- NatWest has failed to engage with them in any constructive way, for more than four years;
- they are yet to have a dialogue with NatWest that will comply with the Mortgages and Home Finance: Conduct of Business Sourcebook (MCOB) 13 (assisting customers in arrears);
- they have set out a payment proposal to NatWest on 4 September 2023 but have had no reply to date;
- NatWest began possession proceedings while Mr and Mrs M were still within the six-month window to bring their complaint to our service. (NatWest has currently put its legal action on hold, pending the outcome of this complaint);
- the investigator's findings aren't supported by any evidence and must be overturned.

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 will explain at the outset that I am not looking at anything that the previous ombudsman decided in his decision of 10 February 2022. I have read his decision and I agree with his conclusion that NatWest had not agreed to switch the mortgage to interest-only and so Mr and Mrs M's decision to pay only the interest has resulted in substantial arrears. It is

simply not up to borrowers unilaterally to vary the terms of their mortgage contract, so this mortgage is, and always has been, a capital repayment mortgage.

NatWest is entitled to set its own lending criteria. Decisions that NatWest makes in respect of what those criteria are, its attitude to risk involved in this particular lending assessment, and whether it should lend and if so, on what terms are clearly discretionary matters for NatWest's own commercial judgement that I would not interfere with.

I'm satisfied that, since the ombudsman's decision, NatWest has considered an application to switch the mortgage to interest-only. Mr and Mrs M say that they met the income and loan-to-value ratio (LTV) criteria for this to be done. However, those are not the only criteria NatWest needs to consider.

There are regulations in place that have flowed from the Mortgage Market Review (MMR) carried out by the FCA which took place after the financial crash in 2008. This has led to a series of major changes, effective since 2014, in the way residential mortgages are regulated. MMR regulations have brought about requirements for stricter lending assessments, aimed at protecting consumers and encouraging mortgage lenders to act more responsibly.

The FCA recognised though that existing borrowers who wanted to make changes to their mortgages might have difficulties with this if they had passed tests under the old rules but wouldn't under the new ones. So, it introduced certain rules to address this.

MCOB says a lender doesn't have to carry out an affordability assessment if a borrower wants to vary or replace an existing mortgage and there is no additional borrowing (other than for product fees) and no change to the terms of the mortgage that is material to affordability.

This means there are two routes that an application for an existing borrower can go down. If there's no change to the terms of the mortgage contract material to affordability, there's no obligation to carry out an affordability assessment at all. And if there is a change to the terms of the mortgage contract material to affordability, a lender could still decide to allow an application without an affordability assessment if doing so would otherwise be in the borrower's best interests.

In this case, a switch from capital repayment to interest-only is considered a material change to the mortgage, and so I'm satisfied NatWest was allowed to carry out an affordability assessment and to apply its lending criteria to the application. In addition, the very substantial arrears on the mortgage are also a material factor, because the balance on the account is much higher than it would have been if all payments had been made in full and on time in accordance with the terms of the mortgage contract to which Mr and Mrs M had agreed to be bound.

NatWest has provided information about its lending criteria and about what was taken into account in its consideration of the application. The bank has explained that Mr and Mrs M's credit files show substantial adverse credit information registered against them – which I confirm is unrelated to the mortgage arrears. After considering this information, I'm satisfied that NatWest reached its lending decision fairly, after taking into account all relevant factors, including (but not limited to) affordability, exposure to risk, and Mr and Mrs M's specific circumstances.

Given this, I'm satisfied that NatWest gave fair consideration to this application and so legitimately exercised its commercial judgement when reaching its decision. This means that

there is no basis upon which I can find that NatWest has treated Mr and Mrs M unfairly or unreasonably.

I'm not persuaded that NatWest was obliged to agree the switch to interest-only in the best interests of Mr and Mrs M; they do not appear to have any strategy for repaying the mortgage arrears over the remaining term of the mortgage, and again this is a factor which is material to affordability.

I'm also not persuaded NatWest has failed to follow either MCOB 13 (quoted by Mr and Mrs M) or the obligations under the Mortgage Charter (which is a voluntary code most mortgage lenders have signed up to in order to help borrowers in financial difficulty). The Mortgage Charter is to help borrowers who are up-to-date with payments but are struggling with the cost of living. However, Mr and Mrs M are substantially in arrears with their repayments.

MCOB allows a lender to switch borrowers to interest-only on a temporary basis in order to help during short-term financial difficulties. There is no evidence to suggest Mr and Mrs M's financial difficulties are temporary, and, in any event, they have unilaterally only been paying interest for the last four years, in breach of the capital repayment mortgage contract.

In relation to other alleged breaches of MCOB, Mr and Mrs M say that NatWest hasn't considered a term extension, that its decision to take legal action is unreasonable while there are so many unexplored options, and that MCOB provides that they should be given sufficient time to sell the property.

Mr and Mrs M have made the following proposals to NatWest's solicitors.

1. convert the mortgage to interest-only and they agree to sell the property "*before the age of 70*" (which Mr and Mrs M incorrectly claim is "*the existing NatWest product*"); or
2. extend the mortgage term on a capital and interest repayment basis so they pay it off at £5,000 per month.

However, Mr and Mrs M haven't applied for a term extension, and to be clear, I wouldn't expect NatWest to put matters on hold if they decided to do so. That's because the court has powers to grant a suspended possession order on the basis of payment of the current monthly instalment, plus an amount off the arrears. In the event the matter proceeds to a court hearing, Mr and Mrs M would then be able to put any payment proposals to the court.

However, a term extension on a capital repayment basis with Mr and Mrs M paying only £5,000 per month doesn't take into consideration interest rate fluctuations. In addition, a term extension would require NatWest to consider affordability, given that this is a material change to the contract.

The adverse credit NatWest noted on Mr and Mrs M's credit files on their previous application for an interest-only mortgage would therefore also have a bearing on any application for a term extension. (In this regard, it is always open to Mr and Mrs M to obtain copies of their own credit files from any of the credit reference agencies, if they want to know what information is recorded on these.)

NatWest isn't obliged to wait until six months after the final response letter before starting legal action. Nor is the bank obliged to put matters on hold while we look at a complaint. Although lenders will usually agree to do so, they don't have to, and we can't force them to. If we had that power, it could also create the potential risk of borrowers in arrears bringing complaints to us with the deliberate intention of halting court action that the lender is

legitimately entitled to take. I do not wish to alarm Mr and Mrs M, but I would not want them to be under any misunderstanding that we would tell NatWest that it must suspend any recovery action in the event of a new complaint being raised.

Mr and Mrs M say that NatWest hasn't made reasonable efforts to reach an agreement over how Mr and Mrs M will pay any shortfall. But, from what they've told us, Mr and Mrs M's position is that there are no arrears, that these are simply a "*technicality*" because they consider their mortgage to be interest-only. In the face of the steadfastness of this mistaken belief, there has been no basis on which Mr and Mrs M have been open to addressing repayment of the mortgage arrears, until their recent request to extend the term on a capital repayment basis and to pay £5,000 per month, without any evidence in support of how this would be affordable, or how they would pay off the very substantial arrears that have accrued over the last four years.

Overall, I'm not persuaded NatWest has acted unreasonably or unfairly – either in its decision to decline to switch the mortgage to interest-only, or in considering any other options to recover the very substantial arrears owed to the bank.

I know this isn't the outcome Mr and Mrs M were hoping for. I can see from what they've told us that Mr and Mrs M believe their mortgage is interest-only, in the face of all the evidence to the contrary. I'm not persuaded that NatWest is responsible for Mr and Mrs M holding this mistaken belief, because the bank has always been very clear that this is a capital repayment mortgage. It would be remiss of me if I did not remind Mr and Mrs M that NatWest is likely to recommence legal action in the absence of firm proposals, supported by evidence, to repay the arrears within a reasonable period of time.

However, the mortgage isn't subject to any interest-rate product, and so Mr and Mrs M are free, if they wish to do so, to arrange a new mortgage with another lender, as there will be no early repayment charge on redemption of the mortgage to NatWest. If, as Mr and Mrs M say, they meet income, LTV and repayment strategy criteria for a new interest-only mortgage, then, absent any other factors that might affect a new mortgage application (such as adverse information on their credit files), they should have no difficulty in arranging a new mortgage with a lender whose account administration might be more to their liking. It might help Mr and Mrs M in this regard to speak to an independent financial adviser. They can find details of IFAs convenient to them via the FCA website at: <https://fca.org.uk>.

My final decision

My final decision is that I don't uphold this complaint.

This final decision concludes the Financial Ombudsman Service's review of this complaint. This means that we are unable to consider the complaint any further, nor enter into any discussion about it.

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

Jan O'Leary
Ombudsman