DRN-4061231

The complaint

Mr M complains about the interest rate charged on his mortgage with Kensington Mortgage Company Limited. He says that Kensington didn't reduce the interest rate when the Bank of England base rate fell, but increased it when base rate rose.

What happened

Mr M borrowed around £142,000 on interest only terms over 25 years. He took an initial fixed interest rate of 6.54%. After two years, his mortgage reverted to Kensington's standard variable rate (SVR), plus a premium of 1.35% reflecting past financial difficulties.

The terms and conditions say that the SVR will always be no more than 3%, and no less than 1%, above LIBOR. This means the interest rate on Mr M's mortgage is limited to 4.35% above LIBOR (being the 3% maximum for the general SVR in the terms and conditions, plus the 1.35% premium set out in his mortgage offer).

Mr M said that he expected his interest rate to reduce in 2020 when the Bank of England reduced base rate to 0.1%. When his interest rate didn't fall, he contacted Kensington, and was told his rate was linked to LIBOR. Mr M said that he wasn't aware of this, and had never been made aware of the link to LIBOR. He asked Kensington to show the link with LIBOR, and to explain why his rate hadn't changed. He said there was no mention of LIBOR in his mortgage offer.

Kensington said that Mr M's mortgage offer said that his interest rate was the SVR plus a margin of 1.35%. And it said the SVR was linked to LIBOR – subject to a floor of 1% above LIBOR and a ceiling of 3% above LIBOR – and that this was set out in the terms and conditions. It said it reviewed the LIBOR rate every three months, and made any necessary changes to Mr M's interest rate at that time. It said that around the time Mr M first raised this issue, in 2020, his interest rate was 4.4% - which was 0.05% LIBOR plus 3% to give an SVR of 3.05%, plus the 1.35% margin above the SVR set out in Mr M's mortgage offer.

Mr M referred his complaint to us. We initially dealt with the question of whether his complaint was in time. I issued a decision setting out that we could consider the fairness of interest charged for six years prior to his complaint being made. A complaint about the fairness of interest charged before that would be out of time. But in considering the fairness of interest charged in the last six years, we would need to look at all the circumstances of the case – including things that happened more than six years ago to the extent that they were relevant to the fairness of interest charged within the last six years.

One of our investigators then considered the merits of Mr M's complaint. She didn't uphold it, so Mr M asked for his complaint to be reviewed by an ombudsman. He said Kensington had never explained how it calculated his interest rate or why it had varied as it had over the years. He said that Kensington hadn't made it clear in his offer or terms and conditions how the rate would be set.

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's mortgage offer says

> *…we are prepared to offer you a mortgage loan ("Offer") on the terms set out below and in our General Mortgage Conditions Booklet 2004 1st Edition.*
>
> *…*
>
> *The interest rate is a fixed rate of 6.54% for 24 months following the end of the month of completion followed by Kensington's standard variable rate currently 5.80% plus 1.35% currently 7.15%.*
>
> *The terms of this mortgage reflect past or present financial difficulties.*

The General Mortgage Conditions Booklet 2004 1st Edition says

> *We may change the variable rate at any time in our absolute discretion whenever we want (including before any advance is released), provided that the changed rate is never less than 1% or more than 3% above LIBOR rate*

I think this is clear – the mortgage offer says that Kensington will charge Mr M the SVR plus 1.35%, and the terms and conditions booklet says the SVR will be between 1% and 3% above LIBOR. Putting those together, Mr M's interest rate will always be between 2.35% and 4.35% above LIBOR. The mortgage conditions say that the "variable rate" – the SVR – will not be more than 3% above LIBOR, and doesn't prevent the offer adding an additional margin to the SVR when setting the rate charged to Mr M.

Mr M says that the offer wording isn't clear. He says that the use of the word "currently" twice suggests that the margin of 1.35% was variable as well as the variable rate – the offer doesn't say that the margin is fixed. He says difficulties he's had getting Kensington staff to explain what his interest rate is show that the offer isn't clearly worded. I've considered what Mr M says about this. I think the offer says that, from the end of the fixed rate, his mortgage would be on a variable rate. The variable rate would be made up of Kensington's SVR, which at the time of the offer ("currently") was 5.8% plus 1.35%, meaning the interest rate would be at that time ("currently") 7.15%. The interest rate after the fixed rate is made up of two elements:

- *"Kensington's standard variable rate currently 5.8%"*
- *"Plus 1.35%"*

giving a total – at that time ("currently") but subject to change – of 7.15%.

I don't think this suggests that the margin is variable; rather, the total rate is variable because it is based in part on the SVR.

Mr M also says that more recently Kensington has issued mortgage terms and conditions worded in a different way. But I don't think whether it has changed how it describes its mortgages now invalidates how it did so in the past.

Mr M says that the mortgage offer doesn't mention LIBOR. And it doesn't. But the terms and conditions do set out the relationship between the SVR and LIBOR, and the mortgage offer says that the terms and conditions as well as the offer is applicable to Mr M's mortgage. As a mortgage is such an important commitment, it's reasonable to expect borrowers to have read both the offer and the terms and conditions before agreeing to it, and I'm satisfied both form part of Mr M's agreement with Kensington. The offer sets out that Mr M will be charged the variable rate plus a margin, and the terms and conditions set out what the variable rate is – including its relationship to LIBOR.

Mr M also questions why there is a 1.35% margin on the SVR. When he took his mortgage out, Kensington offered mortgages to borrowers who had experienced financial difficulty – these were known as sub-prime mortgages at the time. Because such a mortgage presents more risk to the lender, the interest rate was generally higher. Kensington's standard mortgages were lent at the SVR. But mortgages such as this one (which – as the offer says – "reflects past or present financial difficulties") came with an extra premium on the interest rate. In Mr M's case, the extra premium was 1.35%.

As Mr M's mortgage was taken out many years ago, I can't consider whether it was fair for Kensington to have included the premium. But I'm satisfied that the interest rate has operated in line with what the offer says, and Mr M has in fact been charged the SVR plus 1.35%.

Mr M has referred to a set of explanatory notes included with his mortgage statements some years ago. The notes say

> *If your original mortgage offer was issued on or after 1 June 2006, your interest rate may be based on BBR (Bank of England base rate). Please refer to the terms and conditions of your mortgage for further information regarding interest rate charging.*

Mr M says this is evidence that his mortgage – which was taken out later in 2006 – should be linked to Bank of England base rate not LIBOR, and that he has therefore been overcharged. He says that because the notes say that mortgages "may" be based on base rate, that means they may not be based on LIBOR.

But I don't agree about that. This is a general explanatory leaflet; it's not part of the contract between Mr M and Kensington. It was issued many years after the mortgage was taken out, so isn't relevant to what the terms and conditions say or what they mean.

And in any case it says mortgages issued after 1 June 2006 "may" – not "will be" or "must be" – linked to base rate. Equally, they may not. And so that does not preclude them being based on LIBOR if they are not based on base rate. It also refers borrowers to their own specific mortgage terms and conditions, and as I've said above in Mr M's case the terms make clear that Mr M's mortgage was linked to LIBOR not base rate.

Mr M also says that it's industry standard to link to base rate rather than LIBOR. But that's not correct. At the time his mortgage was taken out and the terms and conditions set, some mortgages were directly linked to base rate, some were directly linked to LIBOR and many were set based on fixed rates or the lender's own variable rate.

Taking all that into account, I'm satisfied that Mr M's mortgage should have been charged at 1.35% above the SVR. Having reviewed the charges Kensington has applied I'm also satisfied that it has in fact charged this amount. While the SVR has varied over time, it has always remained within the range of 1% to 3% above LIBOR as set out in the terms and conditions. Kensington has explained how it has varied the SVR within those parameters over time as its own funding costs have changed.

I’m therefore satisfied that the terms of Mr M’s mortgage are clear, that interest has been charged fairly in line with those terms, and that the interest charged to Mr M within the period I can consider has been set fairly. I don’t therefore uphold this complaint.

Mr M has also raised some concerns about the rate he’s being charged by his new mortgage lender, after Kensington transferred the mortgage. I’ve not considered that as part of this complaint, since it has happened since Mr M complained and is the responsibility of the new lender.

My final decision

For the reasons I’ve given, my final decision is that I don’t uphold this complaint.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr M to accept or reject my decision before 19 October 2023.

Simon Pugh
Ombudsman