

Complaint

Mr T has complained that HSBC UK Bank Plc ("HSBC") incorrectly calculated that he wasn't entitled to a refund of any interest when he asked to settle his loan early.

Background

In October 2019, Mr T successfully applied for a loan for £7,700.00 from HSBC. The loan had an APR of 11.9% and a term of 30 months. This meant that the total amount to be repaid of £8,876.27, which included interest, fees and charges of £1,176.27, was due to be repaid in a first monthly instalment of £296.04 followed by 29 monthly instalments of £295.87.

Mr T contacted HSBC about settling his loan early in June 2021. However, he was unhappy at the settlement figure he was quoted as he was told that he wouldn't receive an interest rebate. Mr T didn't settle his loan at this stage and asked for further settlement quotes in August 2021, September 2021 and April 2022. On each occasion, Mr T was told he wasn't entitled to an interest rebate and decided against settling his loan. He eventually complained about the amount he was being asked to repay.

HSBC investigated Mr T's complaint and didn't think it had done anything wrong when providing Mr T with his settlement figures. In its view, it had calculated the amount Mr T was asked to pay in line with the appropriate regulations. Mr T remained dissatisfied and referred his complaint to our service.

Mr T's complaint was looked at by one of our investigators and in his view, Mr T hadn't paid any extra interest as a result of any error in calculating the settlement figure for his loan as he didn't repay the loan early. So he didn't recommend that Mr T's complaint be upheld.

Mr T disagreed with our investigator's assessment and asked for an ombudsman's decision.

My findings

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

Mr T believes that at the time he requested his early settlement figures he should have had an interest rebate, as it is illogical to have to pay all of the interest on a loan when it is repaid early. On the other hand HSBC said that Mr T wasn't entitled to an interest refund. And while it said that the settlement amount complied with the regulations in place, it hasn't really been able to demonstrate how this is the case.

I've carefully thought about what both Mr T and HSBC have said.

In truth, as Mr T didn't settle his loan in June 2021, August 2021, September 2021 or April 2022 and there remains an outstanding balance, the amount HSBC asked him to pay is no longer of critical relevance to this complaint. Nonetheless, given it's clear that Mr T still feels strongly about this matter, I've looked into the amount HSBC asked Mr T to pay in

order to settle his loan early and whether this was worked out in accordance with the applicable early settlement provisions.

The rules regarding early settlement

I think that it would help for me to start by explaining that Section 94 of the Consumer Credit Act 1974 allows a borrower to settle a regulated credit agreement – such as Mr T's agreement with HSBC - and discharge their indebtedness early. And where a consumer requests to settle a credit agreement early, like Mr T requested to do here, the Consumer Credit (Early Settlement) Regulations 2004 ("the regulations") set out how a lender should work out what the customer needs to pay in order to settle the amount outstanding.

Section 5 of the regulations allows a lender to calculate a settlement for (and valid until) a date 28 days after the request for a settlement figure was made. And interest would be charged for this 28-day period. Furthermore, if the agreement in question has a term for longer than a year, like Mr T's two and a half year agreement did, section 6 of the regulations allows the lender to defer the settlement date, for the purposes of calculating an interest rebate, by a further 30 days.

Therefore, as Mr T's request was a request to settle an agreement which had an original term of longer than one year early, the regulations permitted HSBC to charge interest for a period of 58 days from the date of the settlement request.

Amortisation - how loan repayments are applied to outstanding balances

It's important to note that all loans – irrespective of whether interest is added upfront or on a daily basis - are based on an amortisation schedule where each instalment is made up of some of the interest and charges and some of the capital advanced. And this usually means that even though a monthly payment may appear relatively large - in proportion to the amount borrowed - a much smaller proportion of this payment goes to repaying the capital in the early stages.

So many consumers in Mr T's position may believe that they've paid off more of their loan than they have due to the cash amount of the total payments made, because they're unaware of the way that their loan would be amortised and a larger proportion of the early payments were going towards the interest.

In Mr T's case, only £219.77 of his approximately £296 initial monthly repayment went towards repaying the capital balance. And £76.27 of his first monthly payment went towards the interest that had accrued. The proportion of Mr T's second payment that went towards interest was £67.12 as the capital balance owing was £7,480.23, which is £219.77 less than it was at the start.

As the amount Mr T owed reduced with each payment he made, the proportion of his payments that went towards repaying interest also reduced. I appreciate that Mr T says that he wasn't notified about any of this or provided with a breakdown of how the interest would be apportioned when he took out his loan.

However, the loan agreement Mr T signed does state that interest would be added upfront. And as the method used to amortise Mr T's loan was in line with how most loans of this type operate, I wouldn't have expected HSBC to take any additional steps to highlight the schedule or breakdown what proportion of each of Mr T's payments were going to capital and what proportion were going to interest.

Equally, having looked at the amortisation schedule used, I'm satisfied that there were no issues with HSBC's calculations up until March 2020. The situation changed when Mr T had pandemic payment deferrals and I'll now explain how and why this happened.

Mr T's three-month payment deferrals in April 2020 and September 2020 the effect it had on the outstanding balance going forward

As I understand it, Mr T successfully applied for pandemic payment deferrals in April 2020. As a result he, with HSBC's agreement, didn't make loan repayments in April 2020, May 2020, June 2020, September 2020 (the payment made in September 2020 was August 2020's payment taken on the first available working day), October 2020 and November 2020. It's worth noting that the regulator's guidance did permit lenders to charge interest during any pandemic payment deferrals.

Although this wouldn't have made any difference to the total amount Mr T had to pay had the loan run to term because HSBC simply added six extra payments at the end of the term to account for the six deferred payments. Nonetheless by the time Mr T resumed his loan repayments in July 2020, the amortisation schedule was thrown out of kilter by the fact that interest would have accrued on a balance that hadn't reduced in line with the initially proposed schedule.

From what I can see, HSBC appears to have tried to correct this by apportioning £251.29 of Mr T's July 2020 payment towards interest. And it attempted a similar solution with December 2020's payment when it apportioned £238.71 of this payment towards interest. This may well have been what the total interest amount for Mr T's combined April 2020, May 2020, June 2020 and September 2020, October 2020 and November 2020 payments would have been. And I can to some extent understand why HSBC did this.

However, this served to apportion a much smaller amount of Mr T's payment to the outstanding balance. And I don't think that things were ever readjusted in a way that brought the balance back in line with the initial schedule – particularly as the amount going towards interest was even more than what it was right at the start of the loan when the capital owing was at its highest.

I think that this resulted in higher proportion of Mr T's monthly repayment being allocated towards interest rather than reducing the capital going forward.

The position when Mr T asked to settle his loan early in June 2021, August 2021, September 2021 or April 2022

As I've explained, the fixed-sum nature of Mr T's loan, which meant that no further interest could be added, meant that the failure to return to the initial amortisation wouldn't have been a problem or cost Mr T more had he repaid his loan in 30 monthly instalments - albeit repaying his final instalment in October 2022. But Mr T asked to settle his loan early in. And when he did so he was faced with 58 days' worth of interest being added to an unexpectedly larger outstanding capital balance.

HSBC's calculations don't appear to have corrected for this. And while, for reasons I've already explained, I don't agree that Mr T was entitled to an interest rebate of 50%, I don't think that HSBC's settlement figure is correct either.

I fail to see how outstanding balances of £5,029.79 (in June 2021), £4,438.05 (in August 2021) and £2,366.96 (in April 2022) on a loan on an amortisation schedule and being settled early wasn't eligible for an interest rebate when the loan had an APR of 11.9%.

Indeed HSBC's early settlement calculations show that Mr T had no more interest to pay from August 2021, despite having only made 13 payments and still having a further 17 to make and the loan having an APR of 11.9%. I'm afraid that HSBC's numbers simply don't add up here.

Why what Mr T's settlement figure should have been in June 2021, August 2021, September 2021 or April 2022 isn't critical to the outcome of his complaint

Mr T didn't pay an increased amount to settle his loan. He declined to do so when told how much HSBC thought he needed to pay to settle his loan in June 2021, August 2021, September 2021 and April 2022. Mr T says that he had the funds to settle his loan early and would have done so had he been provided with a correct settlement figure.

However, for reasons I've already explained, Mr T incorrectly believed that his settlement amount should have been lower than what it should have been. So I can't reasonably reach the conclusion that Mr T would have settled his loan had he been provided with a correct settlement figure, given he was always likely to disagree with the amount he would have been asked to repay even if the amount had been calculated correctly.

In any event, and perhaps even more importantly it's only fair and reasonable for me to ask a respondent firm to compensate a consumer for financial loss that they actually suffered, rather than a loss that they could have but did not end up suffering. Mr T is effectively asking us to place him in the position that he would have been had he settled his loan in June 2021, August 2021, September 2021 or April 2022.

But the fact remains that Mr T didn't settle his loan early and therefore didn't overpay – notwithstanding the fact that he may have had the funds at this time. For the sake of completeness, I'd add that Mr T hasn't provided me with anything that clearly demonstrates that he did have the funds to repay the loan at the time.

So I'm therefore satisfied that Mr T didn't suffer a financial loss as a result of HSBC's failure to provide him with correct early settlement figures June 2021, August 2021, September 2021 and April 2022.

In these circumstances, I see no value to asking HSBC to retrospectively calculate this amount at this stage and I make no direction in regard to this matter.

Furthermore, as an alternative, Mr T has argued that his loan should be closed as completed and settled. However, I understand that Mr T's loan was closed to recoveries with an unpaid balance of £1,183.48 in April 2023. It's important to note that this means that given the total interest on the loan was £1,176.27 and the remaining balance is greater than this, Mr T still hasn't repaid the capital balance.

As this is the case, I can't reasonably say that this represents Mr T's loss for HSBC providing an incorrect settlement figure either. And I'm satisfied that requiring HSBC to write off the outstanding balance and record the loan as settled wouldn't be fair and reasonable given the circumstances here – in my view this would place Mr T in a far more advantageous position than he would be in had things gone as they should have done.

So overall and having considered everything, I'm therefore satisfied that Mr T hasn't lost out because HSBC didn't provide him with correct settlement figures June 2021, August 2021, September 2021 and April 2022. As this is the case, I'm not upholding Mr T's complaint.

I appreciate that this will be very disappointing for Mr T – as he clearly feels strongly about this matter. But I hope he'll understand the reasons for my decision and that he'll at least feel

her concerns have been listened to – particularly as he has now had an explanation of how early settlement calculations work and how his settlement amounts should have been calculated at the respective times.

My final decision

For the reasons I've explained, I'm not upholding Mr T's complaint.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr T to accept or reject my decision before 3 November 2023.

Jeshen Narayanan
Ombudsman