Financial Ombudsman Service

complaint

Ms R complains that she was mis-sold an interest only mortgage by an authorised representative of Sesame Limited.

background

Ms R previously owned a property, subject to a mortgage. She decided that she wanted to move and approached Sesame for mortgage advice. She was at this time in her mid-fifties.

Exactly what happened next is disputed. However, Ms R ended up with an interest only mortgage over a term of nine years. She says that she told Sesame that she wanted a capital repayment mortgage – and indeed that is recorded as her preference in the fact find.

However, she says that she also asked about lifetime interest only mortgages – one had just been taken by her sister – and she says that she understood that that was what had been arranged for her.

As she was approaching the end of the term the lender wrote to her asking how she intended to repay the capital – Ms R says that it was only at this point that she understood that a fixed term (rather than lifetime) interest only mortgage was what was arranged.

There was no repayment vehicle set up in connection with this mortgage. Ms R has no means of repaying the capital. Sesame recorded on its file that she had an endowment policy projected to pay back £35,000 – this is not correct; Ms R has a small policy, but projected only to pay about £2,000. Even if it were correct, that would only cover about half the capital balance.

Ms R complained that the mortgage was mis-sold. Sesame didn't originally uphold the complaint, but when it came to this service it offered a settlement. It calculated what the balance would be had Ms R taken a repayment mortgage, and calculated the difference between the payments she would have made and the payments she actually made under her interest only mortgage. It calculated that the cost of the mortgage would have been about £53,000 more, but that she had paid about £46,000 less in repayments over the life of the loan. It therefore offered £7,000, being the difference between the two.

Ms R rejected that offer, saying that it would still leave her unable to pay back the capital balance without selling her property. She says that property prices have fallen and her property is now only worth about the same as the mortgage balance, compared to the equity of over £20,000 she had when she started.

Our adjudicator recommended that Ms R accept the offer, but I took a different view, and so I issued a provisional decision. This allowed all parties to draw to my attention any further matters they wanted me to take into account in making my final decision. In responding to my provisional decision, Ms R provided further evidence of the valuation of her property.

Based on this I issued a second provisional decision refining my proposed redress.

my provisional decisions

In considering the sale of interest only mortgages, the key question is whether the mortgage was suitable for Ms R's needs. I wasn't persuaded, in this case, that it was.

In her answers to the fact find, as recorded on Sesame's file, Ms R made it clear that she wanted a repayment mortgage. She described her preference for this as "100%", compared to "1%" for interest only.

While I can't see that an affordability calculation was carried out at the time, it was clear to me that a repayment mortgage wouldn't have been affordable for Ms R. Given her age, and to avoid a mortgage stretching a long way into her retirement, a short term would have been necessary – but this would have increased the repayments to two thirds or more of her gross monthly income.

Whether for that reason or for some other reason, an interest only mortgage was in fact arranged. However, the advice letter says "You informed me that you wish to arrange your mortgage a Capital and Interest basis and I have acted on your instructions" (sic). But the advice letter enclosed a key facts illustration for an interest only mortgage. Sesame says that there must have been an error in the letter on the adviser's part. But there is no other record of what advice was given.

As regards a repayment vehicle, Sesame has recorded that there was an endowment policy worth about half the mortgage balance – in fact, it was only projected to be worth £2,000. It isn't clear what the source of that incorrect information was, but in any event, no consideration seems to have been given to repayment of the other half of the mortgage.

I was satisfied that an interest only mortgage wasn't suitable for Ms R. The term ended when she retired. She had no savings or other investments able to repay the capital. Given the nature and size of the property and Ms R's circumstances, sale of the property wasn't realistic. It wouldn't have raised enough for Ms R to downsize; selling to repay the capital would have resulted in her spending her retirement in rented accommodation.

I was also satisfied that Sesame didn't properly explain to Ms R what she was taking on.

There appeared to have been discussion of three separate and distinct product types – repayment mortgages, fixed term interest only mortgages, and lifetime mortgages. Ms R was given contradictory and misleading information about what type of mortgage she had.

I considered that the right advice to have given Ms R was that she should not have applied for a mortgage. A repayment mortgage wasn't affordable, she wasn't eligible for a lifetime mortgage, and had no way of repaying the capital at the end of an interest only mortgage.

I was satisfied that, had she been given that advice, she would have acted on it – by not taking out a mortgage.

I was therefore minded to uphold this complaint. I then went on to consider redress.

I wasn't persuaded that Sesame's offer was adequate or appropriate in this case. In approaching redress, I took as the starting point that this service aims to put a consumer back in the position they would have been in had nothing gone wrong. Sesame's offer took as the starting point that Ms R would have taken a repayment mortgage – but I didn't think that was the case.

But in any event I didn't think it possible simply to put Ms R back where she would have been. As I have said I considered that, properly advised, Ms R would have done nothing.

That meant she would still be in her old property and now close to paying off her previous mortgage. Instead, she is in a new property with a significant outstanding balance. That can't be unwound.

Directing Sesame to pay off the mortgage capital balance at the end of the term would return Ms R to the position she would have been in in that she reaches retirement age owning a property outright. But it would be a more expensive property, and therefore would leave her in a better position – and wouldn't be fair to Sesame.

Nor, it seemed to me, would Sesame's offer be fair to Ms R. Its starting point was that she would have taken a repayment mortgage – which, for the reasons I have given, seemed to me to be the wrong starting point. By factoring in the amount saved in lower outgoings, Sesame has reduced the redress down to about £7,000. But as Ms R pointed out, this amount would have little effect on her ability to repay the mortgage at the end of the term.

And I wasn't persuaded that factoring in notional savings she hasn't made from a repayment mortgage she would never have taken was appropriate.

I did think that payment of a lump sum to Ms R is the right way forward. But I approached the calculation of that sum in a different way.

Had Ms R remained where she was, she would have owned outright, at the end of the term, a property. I was minded to make redress in this case by directing Sesame to ensure that she has the same value equity, albeit in the new property, at the end of the mortgage term.

Had things not gone wrong she would have had an asset – her old property, owned outright. To make redress, I proposed to award her an asset of equivalent value – an amount of equity in her new property. The effect of this is that I proposed to direct Sesame to pay to Ms R a lump sum that would reduce the value of her outstanding mortgage – increasing her equity to the required level.

In replying to my first provisional decision, Ms R provided me with a valuation of her property, and it was this that I used to calculate the redress I set out in my second provisional decision.

Her house was valued at £80,000 – which was 97% of what she originally paid for it. I didn't have a current valuation for the old flat, but thought it reasonable to estimate that it, too, was now worth 97% of what Ms R sold it for - £49,000. I therefore took that as the starting point for redress; had nothing gone wrong in this case, she would now have an asset valued at £49,000.

In fact, she has a property worth £80,000 with a £66,000 interest only mortgage on it. This leaves her with equity of £14,000, and so a payment of £35,000 is required to put Ms R back in the position of having a £49,000 asset. To that I proposed adding the fees she paid of £1,554.

the responses to my provisional decisions

Ms R responded to my first provisional decision with the valuation set out above. She also said, in responding to my second, that my proposed redress would leave her with a mortgage of around £30,000 to pay off – and given her age and circumstances, she does not see how she could do so. She is concerned that she will still lose her home, and that downsizing would be difficult or impossible, and costly.

Sesame did not respond to my second provisional decision. In responding to my first, it said that my proposed redress was too generous, and in particular that it didn't take into account that Ms R had a responsibility to check her mortgage statements and so should have complained sooner.

my findings

I have considered all the available evidence and arguments to decide what is fair and reasonable in the circumstances of this complaint. I have also considered again my provisional findings in light of the responses to them.

I remain unpersuaded that my proposed redress is too generous. For the reasons I have given, I consider that – as far as is possible – it restores Ms R to the position she would have been in had nothing gone wrong. I can't unwind the property sale and purchase, but I can at least ensure that Ms R's assets remain of equivalent value.

Nor do I think that I should make any discount for Ms R's failure to complain sooner. Ms R understood that an interest only lifetime mortgage had been arranged, not a fixed term interest only mortgage – it is therefore reasonable that this came to her attention when the lender asked about her proposals for repaying the capital balance. In any event, I don't consider that it would have made any difference had Ms R noticed and complained at an earlier stage. Whenever she did so, she would have still have had an interest only mortgage with no prospect of repaying the capital balance. And that balance would still have been the same.

I do have sympathy with Ms R's situation. I understand that she feels that my proposed redress would still leave her in a very difficult situation. But I have to be fair to all sides, and if I were to direct Sesame to write off the entire balance, she would be left in a better position than when she started, with a mortgage free house instead of her flat. I can't advise her as to what options may be open to her when the mortgage comes to an end, but I do urge her to take advice – it may be, for example, that she is now eligible for a lifetime mortgage.

my final decision

For the reasons I have given, my final decision is that I uphold this complaint and direct Sesame Ltd to pay Ms R:

- £35,000 redress;
- £990 lender product fees (which were added to the loan), to which should be added interest at the mortgage rate from the start of the loan running to date of settlement of this complaint; and
- £564 other fees, to which should be added simple interest at 8% running from the start of the loan to date of settlement of this complaint.

If Sesame considers that it should deduct income tax from the interest element of my award, it should give Ms R the necessary certificate.

Simon Pugh
ombudsman