DRN-4765629

The complaint

Mr and Mrs W complain that Pepper (UK) Limited trading as Engage Credit is moving the basis of interest on their mortgage from LIBOR to Term SONIA without their consent.

What happened

Mr and Mrs W took out their mortgage in 2007 with another lender – it's since been transferred to Engage. They borrowed around £135,000 on interest only terms over 25 years. The mortgage offer said that interest would be charged at a variable rate:

- 1.89% above 90 day LIBOR with a discount of 1.55% - giving an effective rate of 0.34% above LIBOR – until 28 February 2009; followed by

- 1.89% above 90 day LIBOR with no discount for the remainder of the mortgage term.

The interest rate would be adjusted on 1 January, 1 April, 1 July and 1 October each year to reflect changes in the LIBOR rate at those times.

LIBOR – the London Interbank Offered Rate – was an interest rate often used in the banking industry to measure the cost of providing funds, and as such sometimes (as in the case) used as the basis of mortgage lending.

However, in 2019, the regulator the Financial Conduct Authority (FCA) announced that LIBOR would be withdrawn. It said that lenders who retain LIBOR-linked mortgages would have to replace the LIBOR element with an alternative. Alternatives included synthetic LIBOR (a projection of what LIBOR would be if it continued to exist), a new rate known as SONIA (Sterling Overnight Index Average), and the Bank of England base rate.

The FCA said that this would require changes to the individual mortgage agreements with borrowers. In making those changes, firms should comply with the terms and conditions of their own mortgages, notifying borrowers and seeking consent to the change where appropriate. But the FCA also noted that because LIBOR was being withdrawn ultimately mortgages would have to be amended even if individual borrowers didn't consent – because lenders couldn't continue to charge interest based on a rate that no longer existed.

Engage wrote to Mr and Mrs W notifying them that LIBOR was being withdrawn, and seeking their agreement to amend the mortgage terms to replace LIBOR with SONIA – the mortgage would continue to operate in exactly the same way, but the interest rate would be calculated as 1.89% above SONIA rather than 1.89% above LIBOR. As the LIBOR and SONIA rates were comparable, Mr and Mrs W would not lose out from the change.

Mr and Mrs W refused to consent. Engage wrote to them several times, and each time they refused to consent.

As a result, Engage did not switch the mortgage to SONIA. But as LIBOR no longer existed, it couldn't continue on that basis either, so instead it used synthetic LIBOR as the direct replacement for LIBOR.

However, synthetic LIBOR was only ever intended to be a stopgap, and when it too came to an end, Engage then had to move the mortgage to another benchmark rate. It again asked Mr and Mrs W to consent to move to SONIA. But they refused to consent again. Engage said it had no alternative, because LIBOR and synthetic LIBOR no longer existed, but the adjusted SONIA rate it proposed to use would ensure that Mr and Mrs W were not going to be charged more than they would have been on LIBOR or synthetic LIBOR.

Mr and Mrs W complained that Engage had changed their mortgage without their consent. They said it wasn't fair Engage hadn't made any other interest rates available to them. And in the absence of a lower fixed rate they wanted their mortgage to track Bank of England base rate, not SONIA.

Our investigator didn't think Engage had acted unfairly, so Mr and Mrs W asked for an ombudsman to review their complaint.

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've set out above the background to the issues in this complaint, around the withdrawal of the LIBOR rate.

The regulator, the FCA, issued guidance to mortgage firms. It said that where appropriate firms should seek borrowers' consent to change the basis of their interest rates. But ultimately, once LIBOR has been withdrawn, it can no longer be used to set mortgage interest rates. So even if borrowers don't consent, firms would have to replace LIBOR with one of the other benchmarks. Firms should try to ensure customers are not worse off as a result of the change.

There's no provision in Mr and Mrs W's mortgage terms and conditions explicitly allowing Engage to change the terms and conditions without Mr and Mrs W's consent. The mortgage could be changed by consent even if there wasn't a term allowing changes.

But their mortgage was LIBOR based. Once LIBOR ceased to exist, there would be no means of calculating the appropriate interest rate. So the mortgage would have to be changed to use another benchmark, even if – strictly speaking – doing so wasn't covered by the terms and conditions. The withdrawal of LIBOR couldn't have been foreseen, and allowed for in the terms, when the mortgage was entered into in 2007.

I'm satisfied Engage has followed the FCA's guidance in this case. It repeatedly asked Mr and Mrs W to consent to the change to their mortgage. When they didn't, it maintained the mortgage on LIBOR then synthetic LIBOR. But now synthetic LIBOR has also ceased to exist, a change would have to be made, whether or not Mr and Mrs W consented.

It wouldn't be fair to simply stop charging interest because the benchmark no longer existed, so it's fair for Engage to replace the old benchmark with a new equivalent one. That's what Engage has done by switching the mortgage over to SONIA. Mr and Mrs W's mortgage is now being charged at SONIA plus 1.89% instead of LIBOR plus 1.89%. I think that's fair.

Mr and Mrs W have said Engage should have used the Bank of England base rate instead. But SONIA is a more direct equivalent to LIBOR. And in any case, since the mortgage was switched to SONIA, SONIA has been lower than base rate – so Mr and Mrs W are better off than they would have been had Engage used base rate instead.

My final decision

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 and Mrs W to accept or reject my decision before 6 August 2024.

Simon Pugh
Ombudsman