DRN-4876231

The complaint

Mr and Mrs B complain about what happened when they applied to HSBC UK Bank Plc trading as first direct ("fd") for a mortgage. They said fd withdrew their offer, and they thought this happened because rates had risen significantly.

What happened

In early 2023 Mr and Mrs B applied to fd for a mortgage on a property they hoped to purchase. They said they secured an offer for a 5 year fixed rate deal at a very good fixed rate of 3.94%. Mr B said rates rose not long after this.

Mr B said they were only borrowing a little over 60% of the property value. Their offer was accepted, and the purchase was going ahead. During the purchase, their solicitor, who was also acting for the bank, advised fd of the existence of a covenant restricting sale of the property to people who could show an existing link to the local area. The solicitor also confirmed that in her opinion this did not affect fd's security.

Mr B said fd was extremely slow to respond to this. He sent us a timeline, with attachments showing the discussion between the solicitor and the bank.

Mr B said they were then ready to complete the purchase, but fd withdrew the mortgage offer, saying it did not find the covenant acceptable. Mr B said when he queried why the covenant was unacceptable, fd said it was because it restricted the ability to resell the property in the event of a default requiring repossession. Mr B said that couldn't be right, properties like this sell extremely quickly in his area, and more importantly the relevant district council had confirmed in writing that in the event of repossession it would waive the covenant. So Mr B said the bank's ability to resell would not be affected.

Mr B said there was nothing in any of the literature or in their conversations with the bank, to tell them a covenant like this wouldn't be acceptable. If they'd known that was the case, they would have applied elsewhere. And they didn't think this was the real reason for withdrawing the offer, because the council had removed this hurdle.

Mr B didn't think the bank had treated him and Mrs B fairly, and it had ignored the advice of its own lawyer. Mr B said that fd's awful service at a very late stage in the transaction nearly caused the whole thing to fail, and it was only because a family member stepped in at the last minute that the purchase could go ahead.

Mr B said he thought fd was just trying to pull as many low interest rate deals as possible, at a time when rates were rising. And he said when he and Mrs B can eventually apply to mortgage the property, they will have to pay much higher rates.

Mr and Mrs B wanted their original loan offer to be reinstated, or a better offer issued if fd now has better rates. They wanted compensation from fd, of rather more than the £250 it had paid. And they wanted fd to cover the additional costs of their future borrowing.

fd said it didn't think it was told about this restriction at the outset. It said that its residential

lending policy does mean properties with occupancy restrictions aren't acceptable security. It said that although Mr B had indicated the local council would waive this on repossession, that doesn't remove the covenant, so fd still wouldn't lend. fd accepted its initial response to the solicitor's query about the covenant wasn't clear, and it apologised for that. fd said it would pay back Mr and Mrs B's £490 booking fee, and it paid £250 in compensation.

fd said it wouldn't waive its policy on the strength of what Mr and Mrs B's solicitors had told it. And it wanted to reassure them that any change in interest rates hadn't caused it to withdraw its offer. This decision was just about the covenant.

When this case came to our service, fd said it had reviewed the case, and now thought it should have paid more compensation. It offered Mr and Mrs B an extra £500, in addition to what it had already paid.

Mr and Mrs B didn't want to accept that. They said they still wanted to know why they weren't warned in advance about any potential conditions for lending. They thought they should have been told the full extent of fd's lending criteria in advance. They said if they'd been told about this, or if fd had asked the relevant questions, they could have looked at a different lender. They still didn't believe that the offer was withdrawn because of fd's concerns about its security.

Mr and Mrs B said what fd was saying made no sense, as it appeared to be claiming that any covenant at all could be grounds for withdrawing a mortgage offer. If that was right, applicants really should be told about this at the outset. And if it was an individual decision made in their case, they thought fd's decision was wrong.

Mr and Mrs B said they bought their house without a mortgage, and hadn't yet secured lending on the property. They said they weren't able to do that until they'd owned the property for at least six months.

Our investigator accepted fd had made a mistake here. But he didn't think fd had to set out all the reasons why it might refuse an application before that application is made. He didn't think fd had breached regulatory requirements.

Our investigator couldn't see any reasonable justification for the delays between fd being made aware of the covenant on 24 May, and it declining the application on 23 June 2023. The sale completed on 14 July, and Mr and Mrs B said they didn't have enough time after fd withdrew its offer, to obtain a mortgage elsewhere. They were loaned some money privately instead, and bought the property in case. But our investigator said if fd had refused on 24 May, they still probably wouldn't have had time to secure a mortgage elsewhere. Our investigator said if fd had known about the covenant sooner, it could have given the correct outcome for their mortgage application earlier. Our investigator said he would have expected a solicitor to be aware of this, and make a lender aware as soon as possible.

Our investigator said Mr B wanted to know if fd's policy relates to all or only some covenants. But he said fd had already clarified this, when it said *"I can confirm our current Residential Lending Policy means properties where restrictions on occupancy, e.g., covenants that restrict the period of occupation and/or the type of occupant are deemed unacceptable*." So he thought fd had explained its position.

Our investigator thought fd's revised offer of £750 in total was fair in this case.

Mr B said he and Mrs B wanted this complaint to be considered by an ombudsman. Our service has invited Mr and Mrs B to comment on why they disagreed with our investigator,

but they have not replied. I said I thought it was now appropriate to move to a decision in this case, and I then reached my provisional decision on this case.

My provisional decision

I issued a provisional decision on this complaint and explained why I did not propose to uphold it. This is what I said then:

> Mr and Mrs B said that fd didn't make clear to them that it wouldn't accept a local occupancy covenant when they first discussed a mortgage. It appears, from the correspondence with fd, as if Mr B had understood he had mentioned this occupancy restriction on the property they were seeking to buy, when he first spoke to fd.
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> I think it would have been helpful if Mr B had mentioned this early on. Whenever someone's buying a property which is a little out of the ordinary, it is prudent to mention that to a lender early, to be sure that this won't cause any problems later. But fd says it has checked, and Mr B didn't tell it about the occupancy restriction when they spoke. Mr B hasn't maintained this position since.
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> I don't think fd had to set out all the reasons why it might later decide to withdraw a mortgage offer, when it first discussed this mortgage with Mr and Mrs B. I don't think this would have been practicable.
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> But I think what is important here, is that a mortgage offer like the one fd issued here is usually binding on a bank. That's so that buyers can rely on the offer when they're making a commitment to purchase. So fd can't simply change its mind later, after the offer is issued. I would have to see that fd acted within the terms of that offer, when it later withdrew it.
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> Mortgage offers do usually include a number of conditions. And I can see that the offer fd issued said this –
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> > *This offer is issued on the basis of the information supplied in your application and any further information which we've requested from you as part of considering it. The offer is made on the assumption that title to the property, over which we'll require a first legal charge (or first ranking standard security in Scotland), is good and marketable and free from any matters which might adversely affect our security.*
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> I think this is relevant because, although the solicitor acting for Mr B and the bank didn't think this occupancy restriction would affect fd's security, fd does appear to have reached a different conclusion.
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> And I note that the relevant conditions, issued with the mortgage offer and to which the offer is expressly subject, say this –
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> > *2.3 We can withdraw from the Agreement at any time before First Drawdown, which will mean that the Mortgage Loan will not be available to you, in any of the following circumstances:*
> > *….*
> > *• if any material term or condition of the Agreement and/or Mortgage Deed is not, or cannot be, fulfilled.*
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> So I think that when fd withdrew its offer, it was relying on the above provision, saying a material term or condition couldn't be fulfilled. And that term or condition was the one fd

set out, when it explained the basis on which the offer was made – that the title to the property was *".. free from any matters which might adversely affect our security."*

I understand that Mr B takes the view that the occupancy restriction wouldn't affect fd's security, and he's shown us that the solicitor acting for him and fd said the same. But I think fd is entitled to reach its own view on this. And its general policy of not lending on properties which have an occupancy restriction suggests it has reached the view that these properties are likely to be affected by that restriction.

Mr B also said the occupancy restriction wasn't relevant, because the local council had said it would waive this. I can see the council said it would waive this if the property was repossessed. But in the meantime, fd had said it wouldn't be able to proceed anyway.

I don't think it's fair to say that this qualified offer of waiver from the local council should have resolved the whole issue for fd. The lender would still consider a wide range of issues in assessing security. That's not just whether it could, in the worst case scenario, sell a repossessed property, but also whether Mr and Mrs B could achieve a sale themselves if things became difficult for them. And, although Mr and Mrs B have told us that the housing market in their area is currently buoyant, with sales of occupancy restricted properties happening quickly, that doesn't change the underlying position that there are fewer available purchasers for this property. So, in short, fd's conclusion that this property was not *".. free from any matters which might adversely affect our security"* would still appear to me to be a reasonable one, even if the property could be sold without restriction on repossession.

So I don't think that fd did anything wrong by withdrawing its mortgage offer to Mr and Mrs B, once it was aware of the occupancy restriction. I don't think there's any suggestion here that fd did this because mortgage rates had risen.

But I do think fd delayed unreasonably in doing so. fd hasn't explained why it took four weeks to tell Mr and Mrs B it wouldn't lend on the property they wanted to buy. I think the service fd provided to Mr and Mrs B at this point was very poor indeed. They should have been told that their purchase couldn't proceed almost right away So I think fd caused three to four weeks of delay in its response.

I've thought about the impact of that on Mr and Mrs B. I don't think, if fd had responded promptly to the solicitor's first notification of this covenant at the end of May, that the arrangement of a new mortgage was already clearly out of the question. But if Mr and Mrs B could have secured a new mortgage then, it would not have been at the rate available in April 2023. Industry literature suggests that rates had risen by the end of May, when Mr and Mrs B should have been told this lending wasn't possible.

So if Mr and Mrs B did lose out on the chance to secure a new mortgage because of fd's delay, then the appropriate comparison would be between any rate they could have secured at the end of May 2023, and a rate they have secured since.

I note that, although Mr and Mrs B told us they weren't able to arrange a mortgage in the six months after a cash purchase, they are now well outside of that time period. And they haven't come back to us to tell us that they have applied for a mortgage since.

If Mr and Mrs B had put a new mortgage in place since purchasing this property, I would then have considered whether fd ought reasonably to contribute to any additional costs of that. But without both information on a rate they could have qualified for at the end of May 2023, and, most importantly, a new mortgage in place now, I can't know whether

Mr and Mrs B will eventually suffer any loss because of this. So I cannot fairly and reasonably ask fd to pay anything towards this now.

Given the above, I do think fd should pay compensation to Mr and Mrs B, and I agree that £250 wasn't enough to provide a fair and reasonable outcome in this case. But, in all the circumstances of this case, I do think that fd's revised and improved offer of £750 provides a fair and reasonable outcome to this complaint. So that's what I currently propose to award.

I invited the parties to make any final points, if they wanted, before issuing my final decision. Both sides replied.

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.

fd replied to say it had nothing to add.

Mr B replied to object. He still felt that he and Mrs B hadn't been treated fairly. Mr B stressed that their financial position was good, and said the loan to value of the borrowing they requested was low. So they thought the only issue here was the covenant.

Mr B repeated his assertion that the covenant would not adversely affect fd's security. He said it would have no impact on fd as long as he was not in arrears. He said it could only possibly affect fd if there were arrears and fd needed to repossess (which he said was extremely unlikely) and in those circumstances the council had said the covenant would be waived. So Mr B said he couldn't see how there was any justification in saying that the covenant would adversely affect fd's security, given all of the above. He said any other argument was flawed in legal terms, and he thought fd ought to have reconsidered.

Mr B also said the covenant wasn't out of the ordinary. It was common in his area for properties like this one to have such a covenant applied to them. Mr B said if this was a blanket policy from fd, then it had a duty to make clear to prospective customers that it might refuse such lending. Mr B said otherwise, he couldn't know. He thought the bank should have asked relevant questions about the property, to pick this up, or the valuer should have noted that it could be a problem.

Mr B also repeated his argument that fd hadn't clarified what sort of covenants were unacceptable to it. He said fd still hadn't answered this.

Mr B also wanted to know whether the reasons I'd said I thought fd could withdraw its offer, were arguments put forward by fd, or whether that was just my interpretation. He said the offer was also based on *"…the information supplied in your application and any further information which we've requested from you as part of considering it."*. So he said he wanted to know where this was requested.

Mr B said that fd wasn't treating customers fairly.

I'd like to respond to the arguments Mr B has raised, before turning to the redress he requested. I should stress here that my duty is to determine this complaint *"by reference to what is, in [my] opinion, fair and reasonable in all the circumstances of the case".*

Mr B asked if the provision I'd identified that fd could rely on to withdraw its offer, had been suggested by fd. That argument wasn't put forward by fd here, but I do think it's appropriate,

and in line with the role of our service, for me to consider the full range of circumstances and documentation before me, not just the arguments that either side puts forward.

I explained in my provisional decision that fd needed to consider a range of scenarios when it's thinking about the security for its lending. I understand that Mr B doesn't anticipate any financial difficulties, and I very much hope that remains the case for him. But unforeseen difficulties do arise, and a bank must consider the potential problems in such circumstances. Here, Mr B appears to be suggesting that if he was in arrears, fd could simply repossess, and avoid the covenant. But the relevant rules set out that repossession should be a last resort, so a lender should always seek to avoid that.

That's why I still think it's relevant that this property would have a reduced market, because of this covenant, if Mr and Mrs B did find they needed to sell it themselves. I don't think it's any answer to that concern, to simply say that fd could repossess the property, with the inevitable extra time, and costs to the customer, that this involves.

Mr B has also said that fd should have asked about this property, and should have made him aware that it wouldn't lend on properties with a covenant restricting sale in this way. I think it's important to note here, that Mr B had apparently always known that the property was subject to a restriction on its sale, and appears to have been aware that this might be a concern for a lender.

I have reached that conclusion, because Mr B initially told fd that he had alerted fd to this covenant when he first discussed lending with its mortgage advisor. When fd replied to Mr and Mrs B's complaint, it said it had trawled its records, and Mr B didn't alert it to this issue at the start of the application. I noted this in my provisional decision above, and also said that Mr B hadn't advanced this argument again.

So I do think it's likely Mr B was aware that a lender could be concerned about this covenant. And in those circumstances, I think it's reasonable to expect Mr B to do what he initially said he had done – mention this to the lender at an early stage. So I don't think that what is fair and reasonable in the circumstances of this case does turn on whether fd should have asked about a covenant on this property when it was first discussing lending with Mr B.

Mr B also said fd had never clarified what its objection was, and whether it would refuse to lend on any property subject to any covenant, or just this sort of covenant. I note that our investigator had drawn part of fd's final response letter to Mr B's attention, which is quoted above. Like our investigator, I do think fd has clarified the nature of its concern here.

I'll now turn to the redress Mr B requested.

Mr B said he and Mrs B had since been offered a mortgage by a different lender, a loan of £162,000 over 13 years, with a 24 month base rate tracker at 0.19% over base rate. Mr B said they were borrowing less, because of the reduced time to repay the loan. Mr B said this loan hadn't yet been drawn down

Although the deal Mr B said he had secured is for a shorter period, the rate is variable rather than fixed, and the borrowing less, he still argued that he and Mrs B ought to receive the difference in payments between the loan they sought from FD, and the payments they now anticipate making over the next five years. He said fd should pay this, which he worked out as £16,358.09 over this period.

Mr B said he and Mrs B didn't consider £750 fair or reasonable, and the minimum they would seek was £16,358.09 plus a suitable offer for distress and inconvenience.

I said in my provisional decision that I thought any potential redress in this case could not be based on the lending Mr and Mrs B applied for, in April 2023, but only on any alternative lending they could have secured at the end of May 2023, when I think they should have been told that their lending with fd could not go ahead. I don't think it would be fair to base any possible redress on lending from fd that was discussed earlier in 2023, but which Mr and Mrs B were not ever going to be able to secure.

Mr and Mrs B would also like us to compare the repayments they would have made on a very different mortgage, to the repayments they say they anticipate making now. Again, I don't think it would be fair and reasonable to do so.

I have considered if Mr and Mrs B could have secured a better deal in late May 2023, which otherwise mirrored the borrowing they've told us they've now been offered. But industry literature suggests that the best available tracker (from the lender Mr and Mrs B have now chosen) at that time was at a rather higher percentage over base rate.

For all of the above reasons, I don't think it would be fair and reasonable to ask fd to contribute to any mortgage payments Mr and Mrs B may now decide to make.

I know that Mr and Mrs B will be disappointed, but for the reasons set out above, I haven't changed my mind in this case. I'll now make the decision I previously proposed.

My final decision

My final decision is that HSBC UK Bank Plc trading as first direct must pay a total of £750 in compensation in this case. HSBC UK Bank Plc trading as first direct can count towards that amount, any compensation it has already paid in this case.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr B and Mrs B to accept or reject my decision before 26 July 2024.
Esther Absalom-Gough
Ombudsman