DRN-4118726

The complaint

This complaint is about a secured commercial loan that Mr S holds with Lloyds Bank Plc. He's unhappy that Lloyds hasn't been taking monthly capital repayments since 2008. It was a condition of the loan when it started in 2007 that the first year's payments would be interest-only, after which capital repayments would begin. That never happened and the full debt is now overdue for repayment. Mr S doesn't have access to enough money to clear the debt, and says the loan balance should be written off.

What happened

By way of a provisional decision dated 21 March 2023, I set out my provisional conclusions on this complaint. The following is an extract from the provisional decision.

> "The broad circumstances of this complaint are known to Mr S and Lloyds. I'm also aware that the investigator issued a detailed response to the complaint, which has been shared with all parties, and so I don't need to repeat the details here.
>
> Our decisions are published, and it's important that I don't include any information that might result in Mr S being identified. Instead I'll focus on giving the reasons for my decision, rounding the figures where relevant. If I don't mention something, it won't be because I've ignored it. It'll be because I didn't think it was material to the outcome of the complaint.
>
> **What I've provisionally concluded - and why**
>
> I'll start with some general observations. We're not the regulator of financial businesses, and we don't "police" their internal processes or how they operate generally. That's the job of the Financial Conduct Authority (FCA). We deal with individual disputes between businesses and their customers. In doing that, we don't replicate the work of the courts.
>
> We're impartial, and we don't take either side's instructions on how we investigate a complaint. We conduct our investigations and reach our conclusions without interference from anyone else. But in doing so, we have to work within the rules of the ombudsman service, and the remit those rules give us.
>
> This complaint arose out of one we were already looking into, about the decision not to re-finance the loan; to be clear, I'm not reviewing that complaint here. Initially, Lloyds indicated to Mr S that he had raised this complaint outside the time limits in our rules. It then emailed us on 3 August 2022 to say it had given Mr S referral rights to this service but said the mediation process might benefit from us waiting a little longer before getting involved. It followed that up a couple of weeks later with a final response including a settlement offer. I've taken that as an indication that Lloyds consents to us considering the complaint.
>
> Mr S has pointed to decisions issued by this service on previous complaints, which he says cover similar situations to his. He's referenced one case in particular and

says his case should be decided the same way. Whilst individual complaints might appear similar, the reality is that no two cases are exactly alike, and an ombudsman will always decide a case on its specific circumstances. That's what I'll be doing here, but I'd also observe, just for completeness, that in the complaint Mr S has pointed to as a reference point for his own, the deciding ombudsman didn't find in the consumers' favour.

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint. Having done so, I'm satisfied this case is more straightforward than it might first appear. That's because I don't need to decide whether Lloyds is at fault.

In the final response issued in August 2022, Lloyds has accepted that it failed to switch the loan to capital repayment after the first anniversary in 2008. It'd also offered to compensate Mr S for that omission. What I therefore have to decide is whether the resolution Lloyds offered in that response was enough, or if it needs to do more.

In arguing his case for the outstanding balance to be waived, Mr S has pointed to various elements of the underlying loan agreement, which he believes Lloyds has breached, rendering it unenforceable in law. I should explain that only a court can decide if a loan agreement is legally enforceable. Whilst I am required to take account of relevant law when deciding a complaint, my primary obligation is to decide what is fair and reasonable in all the circumstances.

When I do that, I have to keep in mind that Mr S has benefited greatly from the money he borrowed under this agreement, as it has allowed him to earn a substantial rental income from the commercial property that act as security for the lending. That being the case, it wouldn't be fair or reasonable for him not to have to pay back any of the money he borrowed.

It's also apparent from the historic notes in Lloyds' records that Mr S has been aware of the failure to switch to capital repayments for several years. That's particularly relevant given the nature and subject of the complaint. In essence, Mr S' complaint is one of "under-funding". That's where, for whatever reason, a borrower hasn't paid all of the money that was due under the terms of a loan agreement, as a consequence of which the loan balance is higher than it should be.

Where that happens solely as a consequence of a mistake by the lender, we will, as a starting point, expect the lender to compensate the borrower by adjusting the balance to reflect the additional payments that should have been paid but weren't. But there are several caveats to that.

Firstly, we keep in mind that the borrower has had the benefit of paying less each month than they would have if nothing had gone wrong. We also take into account the possibility that the borrower's payment record at the lower level indicates they might have struggled to pay the full amount they should have been paying. But the single most important caveat relates to when the borrower knew (or should have known – both tests are relevant here) that they weren't paying the full amount they should be paying.

Even though the problem may have arisen due to a mistake by the lender in the first instance, it's reasonable to expect a borrower to take steps to limit the damage once they are aware of it; that's called mitigation. Here, it's a matter of record that Mr S knew in 2018 that Lloyds hadn't been taking the monthly capital instalments.

However, as I said earlier, there are two tests to apply, and in Mr S' case, Lloyds took the view when making its settlement offer, that he should have known there was a problem from the statements he received each year.

I can see why Lloyds might think this to be a fair position to take when arriving at its redress proposal. The first annual statement, from 2008, would have correctly shown the loan balance as unchanged, but Mr S should have been expecting his statement for 2009 to show a reduction, following a year of higher payments. He should, of course, also have been expecting the payments taken from his funding current account by direct debit to be higher in year two. In reaching that conclusion, I've taken account of a couple of key factors.

First of all, the term in the loan agreement requiring capital payments to be made from 2008 onwards was Mr S' condition to comply with; not Lloyds'. It's a universally-accepted convention of lending and borrowing that borrowers are responsible for making the payments required of them under the lending contract. That's not a responsibility that can be delegated or transferred to any other party. Secondly, Mr S is a professional landlord; he's running a commercial business. One of the responsibilities of managing a business is to ensure that any and all business debts are being paid as they should be.

The reality, however unwelcome or unpalatable he might find it, is that Mr S' current position is not solely down to Lloyds' omission in 2008. It's also partly down to him not noticing the omission and taking reasonable steps to remedy it in a timely fashion. The statements Lloyds has sent him over the relevant period mean that Mr S always had enough information at his disposal to realise the loan balance wasn't falling. Given that making the capital repayments was his responsibility, it was up to Mr S to remedy that.

Put all of the above together, and it might seem that the settlement Lloyds has proposed is fair and reasonable, in all the circumstances; but for one thing. Lloyds makes much of the fact that Mr S knew of the problem in June 2018. That's when it was decided mutually to leave things as they were until maturity in 2022 and Mr S would then try and re-finance. But that also means Lloyds knew in 2018 that it had made a mistake in 2008 that had financial implications for its borrower.

Lloyds' note of the June 2018 meeting implies that it suited Mr S to "kick the can down the road", so to speak, until maturity and try to re-finance then. That may be true, and I suspect neither party anticipated in 2018 the difficulties Mr S would have re-financing in 2022. It might even be argued that what was decided in 2018 amounted to a variation in the terms of the contract, albeit an undocumented one. But it seems to me that it was rather disingenuous of the bank not to have offered the one-year's worth of redress it offered in 2022 *in 2018*. If it had applied that then, Mr S would at least have benefited from the effect of the redress during the intervening years.

The main elements of that settlement proposal are that Lloyds would reduce the balance by an amount equal to the first year of capital repayments that should have been made; that's around £20,000. It would also reduce the balance by an amount equal to the interest that would not have been charged over the life of the loan if the first year of capital repayment had been made; that's around £41,000. It's also proposed suspending any interest that would normally be charged during what is described as the "current charging period". Using Mr S' annual statements as a reference point, I'm taking that to mean the period from 1 April 2022 to 31 March 2023; the sum itself is unspecified.

> If that resolution were implemented now, it would reduce Mr S' outstanding balance from just under £403,000 to a little over £341,000. But if it had been implemented in 2018, when I think it should have been, Mr S would have been charged less interest in the intervening years than he has been, because his charging balance would have been £61,000 lower. So yes, Lloyds' settlement proposal is broadly fair, but it should have been offered and implemented in June 2018, giving Mr S the benefit of it during the years since. So, in addition to what is already proposed, Lloyds also needs to reduce the loan balance by the amount of interest that Mr S would not have been charged if Lloyds had implemented the underfunding remedy in June 2018.
>
> If the complaint was eventually to be settled on the terms I am intending to order, Mr S would still owe a substantial sum of money to Lloyds. Furthermore, I'm mindful of the fact that during the time the complaint has been with us, the extended deadline for repaying the balance has now passed. Mr S has told us he doesn't have the money and can't re-finance to another lender.
>
> Going forward, it's for Lloyds and Mr S to have a constructive dialogue about the future of the loan; it's not for this service to say how that dialogue should take place or in any way pre-empt the outcome. But that dialogue needs to happen and I very much hope it takes place without any recrimination over what has gone before. All I'd add is a reminder to Lloyds that its duty to treat its customers fairly is ongoing, and a reminder to Mr S that Lloyds has the right as a last resort to seek to enforce its security in the event a mutually-agreed solution can't be reached."

Both parties were given a two-week time frame in which to make their further comments; that time has now passed, and we've heard from both.

Mr S didn't accept the provisional decision, and submitted further comments and documents, all which I've considered carefully. I've also sent Mr S, as requested, a copy of the record Barclays made of the discussion in 2018, as he said he'd never seen it. In response to that, Mr S has made a further submission aimed primarily at discrediting the authenticity of the record.

Lloyds confirmed its acceptance of my provisional decision, but also provided an explanation of why backdating the proposed underfunding resolution to 2018 would be less favourable to Mr S. Instead, Lloyds proposed implementing the resolution as originally offered in 2022, including refunding all interest charged between April 2022 and March 2023. The combined effect of these would be to reduce the loan balance by £79,093.20. Of that sum, £41,188.48 has already been credited to Mr S' loan account in August 2022, which would leave £37,904.72 still to apply.

The investigator let Mr S know that I considered the offer from Lloyds to be fairer than what I had proposed in the provisional decision. Mr S replied saying he did too, but still wanted his own preferred remedy of a full write-off.

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 considered afresh everything that both parties have said and provided. Mr S has said that he'd like a discussion with me about his complaint before I determine it. That wouldn't be appropriate. It would, in effect, be giving Mr S a one-sided personal hearing to press his case directly without the business being involved and being able to contribute.

On the rare occasions we conduct a direct hearing, it's at the discretion of an ombudsman, is called solely because he or she thinks it's essential to reaching a fair outcome, and both parties to the complaint are present. Anything else would be procedurally unfair, and introduce the risk of bias. I'm satisfied this is a complaint I can fairly deal with on the basis of the evidence on file from the parties.

Mr S has mentioned various documents that he says must be on our file (because without them I could not have reached the concisions I did) and therefore he must be allowed sight of them before the complaint is determined. The document Mr S has referred to most frequently, and placed the greatest importance on, is what he refers to as an "acknowledgement letter". He says that I must have it on file as I've referenced it in the provisional decision.

I've looked very carefully through the provisional decisional decision and can't find any mention of an acknowledgement letter. Indeed, there are only two pieces of evidence that I've specifically referenced in the provisional decision. Those were the loan agreement and Lloyds' record of the 2018 discussion, and I explained the relevance that both had to my findings (all of which is reproduced above). Mr S has had sight of both documents, so I'm satisfied his right to procedural fairness has been met.

At one point in the provisional decision, I referenced "the June 2018 meeting" when talking about the record Lloyds made of the discussion about the problem. In fact, the date of the discussion record is 31 May 2018. That's why I referenced June 2018 as the retrospective date for implementing the redress; whilst it doesn't affect the overall outcome, nonetheless, I apologise for the error in referring to "the June 2018 meeting".

Mr S has gone to great pains to argue that the record of 31 May 2018 is fraudulent. He's told Lloyds he thinks it's a fake, and Lloyds has told us it has set this up as a separate complaint to look into as a new allegation. Mr S has also told us that he has reported the alleged fraud to the police. Fraud is a crime, so that's the proper course of action to take if Mr S thinks a crime has been committed, but the Financial Ombudsman Service isn't a branch of the criminal justice system. In the meantime, having considered everything Mr S has said about why he considers the record of 31 May 2018 to be a fake, I'm not persuaded I shouldn't continue to place the weight on it that I have done up to now.

I say that not least because the record wasn't exclusively about the discussion of what to do about the 2008 failure to switch the loan to capital repayments. It was a wider discussion about other business arrangements Mr S has with Lloyds. Those aren't relevant here but the fact that the record of 31 May 2018 includes those matters as well as the issue of the underfunded loan make it more likely than not that the record is genuine.

In any event, it doesn't really help Mr S' case to dispute the authenticity of the 31 May 2018 record. It is that record that demonstrates when Lloyds became aware it had made a mistake in 2008, and therefore knew it should do something to put the mistake right. Indeed, it's the reason I recommended Lloyds backdate the implementation of the redress offer to June 2018, albeit I have now moved away from that idea, and both parties have agreed that I should.

I did also say that the record of 31 May 2018 showed Mr S to be aware of the mistake as well. I suspect that is what is really behind his efforts to discredit the record. But that argument is irrelevant because I then went on to say why I considered Mr S should reasonably have been aware of the mistake as far back as 2009, when his monthly payments didn't go up and his loan balance didn't begin to come down. Put all that together,

and Mr S' response to the provisional decision challenging the authenticity of the record of 31 May 2018 serves more to weaken his case rather than strengthen it.

In summary, having reviewed the evidence in its entirety, for all the reasons set out above, I'm not persuaded that Mr S' claim for a full write-off of the debt he owes to Lloyds is a fair and reasonable outcome. Lloyds did make an error in 2008, but Mr S – a businessman by profession in his own right – should reasonably have noticed the mistake and drawn it to the bank's attention at the time, or soon afterwards, so that corrective action could be taken.

When the opportunity for corrective action was offered to him in 2018, I'm persuaded by the available evidence that he elected not to take that opportunity. In all the circumstances, and taking account of everything that has been said and provided, I conclude that the current offer from Lloyds to reduce Mr S' loan balance is the fairest solution.

Mr S doesn't have to accept my conclusions, and if he doesn't, then neither he nor Lloyds will be bound by my final decision. Subject to any time limits or other restrictions a court might impose, Mr S' right to take legal action against Lloyds over the subject matter of this complaint won't have been prejudiced by our consideration of it. As I indicated in the provisional decision, a court is the appropriate forum for Mr S to pursue his belief that the loan agreement is unenforceable. He may wish to take legal advice before commencing such action.

My final decision

My final decision is that I uphold this complaint in part. In full and final settlement, I order Lloyds Bank Plc to reduce the balance of Mr S' loan by a further £37,904.82, making a total reduction of £79,093.20. I make no other order or award. My final decision concludes this service's consideration of this complaint, which means I'll not be engaging in any further consideration or discussion of the merits of it.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr S to accept or reject my decision before 6 June 2023.
Jeff Parrington
Ombudsman