complaint

L complains National Westminster Bank Plc (NatWest) mis-sold it an interest rate swap agreement in February 2008.

background

L is a limited company. In February 2008, it consolidated an existing loan and new borrowing into a £950,000 loan. At the same time it took out a swap for the whole loan amount over a 10 year term at 5.35%. In November 2010, it looked into breaking the swap but was told that'd cost £150,000 so it didn't do this.

NatWest reviewed the sale of the swap in conjunction with the Financial Conduct Authority. It offered to put L in the position it'd have been in if it'd taken out a six year swap at a rate of 5.13% instead. L didn't agree and brought its complaint to this service.

I issued a provisional decision saying I was planning to uphold the complaint in part. A copy of my provisional findings is attached and forms part of this decision. In summary, I thought there'd been shortcomings in the information L had been given. But I thought L would've still taken a swap out even if everything had happened as it should – just for five years instead of the six years NatWest had offered; or the 10 years it'd actually taken out.

NatWest replied saying it accepts the provisional decision. L replied saying it doesn't. I've read and considered its response in its entirety. In summary, it said:

- It didn't understand it wouldn't be able to benefit from falling interest rates.

- The call where NatWest mentioned the possibility of taking out a "*ceiling*" was before it was provided with a presentation that explained the key features of a cap. NatWest didn't explain in the call what a ceiling meant. And the use of different terminology over time wouldn't have helped. It didn't have experience of these products and it therefore wasn't in an informed position to reject a cap.

- NatWest positioned a swap as being more suitable than a cap on a number of occasions. It incorrectly said it was a simple product and it didn't provide a balanced view on what interest rates might do – instead it emphasised how unlikely it was that they'd fall.

my findings

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

I think L did understand it wouldn't be able to benefit from falling interest rates with the swap. It was described as being a product that'd fix the interest rate and this was effectively what it did. Although L needed to clarify it wouldn't benefit from falling interest rates in the section of the call it's quoted, it does seem as though it understood this and NatWest confirmed it. And I'm satisfied from the rest of the call and the paperwork L was later given that L would've understood this.

However, as I set out in my provisional decision, I accept L wasn't given enough information to make an informed decision about taking out a swap rather than a cap. And the use of different terminology wouldn't have helped. I also accept NatWest delayed explaining caps in any detail until the presentation and positioned a swap as being more attractive.

But as I explained in my provisional decision, a complaint isn't automatically upheld because there were shortcomings. My role is to go on to decide what the complainant would've done if there hadn't been any shortcomings. I accept L might've chosen to take out a cap if it'd been given all the information it should've been. But taking everything into account, I still think it's most likely that without the benefit of hindsight, L wouldn't have been attracted to a cap.

I say this because the cap premiums NatWest has quoted are reasonably high and in my experience the overall total would've been higher if they were paid monthly. I therefore think L would've only been prepared to pay this if it was attracted to one of the main benefits of caps – either the ability to benefit from falls in interest rates, or the lack of break costs (other than losing any premiums not yet paid).

From everything I've seen, I think L thought it was more likely interest rates would rise. It also explicitly said that even if interest rates did go down, it was happy to accept it'd lose out. It seems this was because it thought it would only be a small fall. L says NatWest didn't give it a balanced view on what interest rates might do. And I accept it may have expressed a belief they'd go down. But no one knew what interest rates were going to do. And ultimately I think L would've known this was simply an opinion and it was up to it to make a decision based on what it thought interest rates would do.

Taking everything into account, I also don't think L was planning to break within the five year term of the replacement swap I set out in my provisional decision. So I don't think the lack of break costs with the cap would've been attractive enough to it to make it want to pay the premium – even when combined with being able to benefit from falling interest rates.

I know this will come as a disappointment to L but my conclusions therefore remain as set out in my provisional decision – I think L would've taken out a five year swap if everything had happened as it should've.

fair compensation

Where I uphold a complaint, I can make a money award requiring a financial business to pay compensation of up to £150,000, plus any interest and/or costs that I consider appropriate. If I consider that fair compensation exceeds £150,000, I may recommend the bank to pay the balance. This recommendation won't be part of my determination or award. It won't bind the bank. It'd be unlikely that L can accept my decision and go to court to ask for the balance. It may want to consider getting independent legal advice before deciding whether to accept my decision.

the specified steps

NatWest should put L in the position it would've been in if it'd taken out a five year swap instead of a 10 year one. It says it would've offered a rate of 5.08% for a five year swap. This requires it to:

- Pay L the difference between what it actually paid and what it would've paid with a five year swap.

- Refund to L any charges or fees it wouldn't have incurred if it'd held a five year swap.
- Pay L compensatory interest of 8% simple a year* on each reimbursed payment from the date it was paid to the date compensation is paid.
- Write off the break cost associated with the 10 year swap.

*If NatWest believes it's legally required to deduct tax from this interest, it should send a tax deduction certificate with the payment. L may then be able to reclaim any tax overpaid from HMRC, depending on the circumstances.

L hasn't explained what consequential losses it feels it's suffered (despite me asking about this in my provisional decision) so I haven't made an award for any consequential losses.

my final decision

determination and award: I uphold the complaint in part. I consider that fair compensation requires National Westminster Bank Plc to carry out the steps specified above. I require it to do this – up to a maximum financial effect of £150,000.

recommendation: if the financial effect of any award exceeds £150,000, I recommend that National Westminster Bank Plc still carry out in full the steps I specify.

Under the rules of the Financial Ombudsman Service, I'm required to ask L to accept or reject my decision before 18 February 2016.

Laura Layfield
ombudsman

COPY OF PROVISIONAL FINDINGS

The loan agreement includes a condition that L "*maintain the interest rate hedging arrangements approved by the Bank*". NatWest says it required a hedging product to be taken out for at least 10 years. It says the fact the internal credit submission only refers to the 10 year term that's been agreed and doesn't say it would've been happier with a shorter term is evidence of this. I've thought about this carefully. But taking everything into account, I don't think I've seen any persuasive evidence that L needed to hedge for 10 years. And in fact, it seems L was presented with five year products.

Inserting conditions for hedging arrangements is something this service is usually satisfied is within businesses' commercial discretion. And I don't see any reason to depart from that here. But I'm not persuaded it was a condition of the loan that L hedge for 10 years. Any compensation I award would therefore have to put L in the position it would've been in if it'd taken a hedging product. But I'm satisfied it's open for me to decide that hedging product could've been for a shorter term than the 10 years L agreed to.

L says it wasn't given enough information about the swap it took out or the other options that were available to it.

I've thought about this carefully. It does seem as though L was presented with various product options – both verbally and in documentation it was sent. But I note it was only quoted the cost of a 10 year cap – despite having been quoted the rates available for both five and 10 year swaps. And L says it wasn't made clear to it that it could pay the premium on a monthly basis rather than having to pay it all upfront.

I also accept L wasn't given enough information about the possible break costs of swaps. I think it was made aware that they existed and could be "*considerable*". But I can't see that NatWest gave L enough information to understand how considerable they could be.

Having decided there were shortcomings in the information L was given, I have to decide what L would've done if everything had happened as it should. It isn't possible to know this for sure. So I have to decide what I think is most likely.

Taking everything into account, I think it's most likely L would've still chosen to take out a swap. But I think it would've chosen to take that out for five years instead of 10.

I say this because from listening to L's conversations with NatWest, I think L was far more concerned with protecting itself against rising interest rates than it was with being able to benefit from falling interest rates. During the initial call in December 2007, NatWest told L taking out a "*ceiling*" might be a good idea for it because this would allow it to benefit from low interest rates whilst protecting against rising interest rates. It told L there'd be a cost for this but didn't expand on this and L didn't ask. Instead L said it'd be happy at around 5.4% and it'd accept that if rates went down it'd lose out. It expressed the view that it was far more likely rates would go up by 2% than fall by 2%.

NatWest has told us five year caps at 6%, 6.25% and 6.5% would've cost L £20,757, £19,403 and £18,336 respectively. Taking everything into account, I think these premiums would've put L off taking out a cap – even knowing it could ask to spread whichever premium it selected over the term of the cap.

In terms of thinking L would've only taken a swap out for five years if everything had happened as it should, I say this because although L thought it wouldn't repay the loan early, it does seem as though this was a real possibility. On several occasions L asked questions about what would happen if it sold up after five years or if it made overpayments to the loan. A five year term would've given L a lot more flexibility and I think this would've been attractive to L.

NatWest offered a six year term under the review. But it seems as though this was based on what break cost would fall within the Financial Conduct Authority's guidelines rather than what it actually thought L would've chosen. As it seems L was offered five and 10 year products at the time I think it's more likely L would've picked a five year term rather than a six year one.