complaint

G is a limited company. It complains that Lloyds Bank PLC mis-sold a fixed rate business loan to the company.

background

G took two fixed rate business loans from Lloyds – the first in 2009 and the second in 2012. The company has complained to this service about both loans and we've considered them as two separate complaints. This decision deals with G's complaint about the 2012 fixed rate loan. There is, however, a great deal of overlap between the events in the two complaints, so my account of the background and findings below will cover both fixed rate loans.

In June 2009, G took a fixed rate business loan for £200,000, repayable over 20 years. The rate was fixed for the first ten years at 6.62% all-in, reverting after that to a variable rate of 2.25% above base rate.

In July 2009 G also took a variable rate loan for £143,000, repayable over 20 years.

In November 2012, G took a further fixed rate business loan for £101,500, again repayable over 20 years. The rate was fixed at 5.055% all-in, for the full term of the loan.

In October 2013, G took a further variable rate loan for £30,450.

G experienced financial difficulties and in late 2014 the bank transferred control of the accounts to its recoveries team. At this time the loans were terminated and the bank charged break costs of £17,582 and £359 on the 2009 and 2012 fixed rate loans respectively.

The bank investigated G's complaints. In the case of the 2009 fixed rate loan, Lloyds said it could have done more to explain the potential size of break costs. It offered to refund the break costs, with interest, and to put the loan on the variable rate from the date of the complaint. In the case of the 2012 fixed rate loan, the bank considered it had provided sufficient information about break costs in 2012, and therefore didn't propose to offer any redress.

Unhappy with the bank's response, G referred its complaints to this service.

G also claimed for consequential losses which it believed it suffered as a result of having the two fixed rate loans. In particular it claimed for the following:

- losses on the sale of equipment
- loss of the licence on which the business depended
- impact on the completion of building works
- impact on the upkeep and development of buildings and facilities
- debts with third parties
- impact on the potential sale of a portion of land and buildings
- a lost deal with a potential investor who withdrew because of the break costs
- compensation for the trouble and upset suffered by G's director because the bank relied on his house as security for the lending

After investigating G's complaints, our adjudicator concluded that the 2009 and 2012 fixed rate loans were both mis-sold. He recommended that G should be put in the position it would have been in if both fixed rate loans had been variable rate loans and G had taken a five-year interest rate cap at 5.0% for £250,000 in 2009. He didn't recommend that G's consequential loss claim should be upheld.

The adjudicator gave these reasons for his recommendations, in summary:

- He didn't think Lloyds had done enough to explain the potential costs of exiting either of the fixed rate loans early. The bank gave examples that weren't specific to the actual loans taken, and didn't explain how to apply the figures to different amounts and loan periods.

- Lloyds said its records indicated the relationship manager in 2012 discussed the features, risks and benefits of a number of products with G's director. But the adjudicator had seen no contemporaneous evidence that the potential scale of break costs were discussed at the time.

- If G had understood the potential scale of break costs, the adjudicator thought the company would still have agreed to some interest rate protection in 2009. No business would be immune to the risk of rising interest rates. And the base rate had fallen from around 5% to 0.5% during the 12 months before G took the 2009 loan. So it was reasonable to conclude G would have seen protection against future rate rises as an attractive option.

- G's business was by its nature subject occasionally to windfall gains, which the company had previously used for development and refurbishment. It would have been reasonable to conclude the company would later be in a position to use similar gains to reduce or repay its loans early. Given its business model, the adjudicator thought G would have selected an interest rate cap in 2009 rather than the fixed rate. A five-year cap would have provided the company with a reasonable period of interest cost certainty. The minimum available would have been a cap covering £250,000 of lending.

- With this cap in place, G would have had around 62% of the increased loan facilities already covered by a hedging product at the time of the 2012 loan. So, on balance, the adjudicator didn't think G would have seen a need for additional protection in 2012.

- Between 2010 and 2013 there was a series of events in G's business, unrelated to the fixed rate loans, which ultimately led to the financial difficulties experienced by the company. G's accounts show that by 2013, overall income had fallen to less than 30% of its former level. For these reasons the adjudicator didn't think the fixed rate loans caused the losses from the sale of equipment, the loss of the licence, the lack of funds to develop and maintain the site and buildings, or problems paying operating costs. Nor was he persuaded the fixed rate loans caused any losses related to the potential sale of land and buildings, or to the security arrangements for the lending.

- There may have been genuine intent to negotiate some kind of deal with an investor. But the adjudicator didn't think he could safely conclude it was the fixed rate loans that caused the investor not to proceed.

G didn't agree with the adjudicator's recommendations. He made the following points, in summary:

- G agreed it wouldn't have taken the fixed rate loans if it had known about the break costs. But nor would the company have taken a cap. The directors wouldn't have taken 'insurance' if they were taking a gamble on variable rates. Some of their business losses had been uninsured. The directors didn't have life insurance (until it became a condition of lending) and, as a further demonstration of taking gambles, they had no pensions, relying instead on the properties to be their pension pot.

- G's director maintains that the available cash from having only variable rate loans could have made the difference between the business surviving and not.

- The prospect of break costs was a deal-breaker for the investor.

After the adjudicator issued his conclusions, the investor submitted a letter to us. In it he says that in 2014 he'd reached a deal with G to develop the business. At the time, one of his conditions was that G should move its accounts from Lloyds to his bank, but he was then told the break costs would be £30,000. He explored restructuring the Lloyds loans as an alternative, but without success. He says this made the deal impossible.

Lloyds also disagreed with the adjudicator's recommendations. The bank thought its original offer was fair and reasonable. It made the following points, among others, in summary:

- Even if G had been given better information on break costs in 2009, the bank thinks G would still have entered the fixed rate loan. It was a long term business plan and rates were at a historic low.

- G already had flexibility in its lending structure. Variable rate lending made up 40% of its debt to the bank. Furthermore, the bank thinks it was unlikely G would have been in a position to pay off its debt to the bank before the end of the first fixed rate period.

- The bank doesn't accept G would have taken an interest rate cap. The bank had no duty to offer a cap, which is a regulated hedging product, requiring a detailed sales process. G had no prior experience of derivatives or interest rate hedging.

- With the benefit of hindsight, it would have been financially better for G to have entered the cap. But that wasn't foreseeable at the time. It's only with the benefit of hindsight that it's possible to say the company would have entered into the cap.

- When the 2012 fixed rate loan was sold, G was given documentation that clearly set out the basis on which break costs could be calculated.

- Ultimately, it can't be said that G wouldn't have taken the 2012 fixed rate loan if it knew it would incur break costs of £359.

- At the time of the 2012 loan, the five-year cap recommended by the adjudicator would have had only two years to run, and the new loan had a 20-year term. G clearly wanted more interest rate protection than that, as evidenced by its decision to enter a 20 year fixed rate.

my findings

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

the 2009 fixed rate loan

It's common ground that G didn't get enough information about break costs during the 2009 sale. It isn't possible to be certain what would have happened if the bank had given G sufficient information, so I need to decide what would have been most likely.

Both parties argue, for different reasons, that G wouldn't have taken a cap in 2009. Lloyds thinks that with more information, G would still have taken a fixed rate loan. By contrast, G says it wouldn't have taken any measures to protect itself from interest rate rises.

Lloyds also says a cap is a more complicated product than a fixed rate loan, with more regulation on its sale, which would have involved an additional department of the bank. But if G had found the fixed rate loan unattractive because of the break costs, I see no reason why the bank wouldn't have offered other products for controlling interest rate risk. I'm not persuaded the fixed rate loan was a good fit for G's approach to business planning, so I agree with the adjudicator that a cap would have been more attractive to G.

My aim here is to put G in the position it would be in if the bank had given all the proper information at the time of the transaction. In my view, replacing the fixed rate with a cap is more likely to do that than is the bank's offer of refunding the break costs and putting the loan on the variable rate from the date of the complaint.

G's argument is that the company was in the habit of taking gambles on such matters and therefore would have embraced the risk of rising interest rates – in other words, it wouldn't have played safe by paying for a cap. I accept that G was an unusual business which, as its director points out, approached some of its decisions in an unusual way. But the interest rate environment in 2009 was also unusual. Rates had fallen steeply and no one knew what would happen next, so there would have been a persuasive case for some kind of hedging – even for a business like G. On balance, I think G would have taken an interest rate cap. I think the company would have regarded five years as a reasonable period of certainty.

For these reasons, I'm satisfied that replacing the ten-year fixed rate with a five-year interest rate cap is a fair and reasonable outcome of G's complaint about the 2009 loan.

The adjudicator recommended that the cap should run from the date of the July 2009 variable rate loan. I think that's reasonable. Otherwise, the £250,000 notional amount would have exceeded the lending during the short period between the two 2009 loans.

the 2012 fixed rate loan

The information G received before the 2012 loan was different from the information in 2009. Even so, I agree with the adjudicator that G's director still wouldn't have been able, from this information, to grasp the potential scale of break costs on the loan. And it's the potential costs that are of relevance here, not the actual break costs incurred in the particular circumstances of 2014 when the loan was terminated.

Again, I need to decide what's most likely to have happened if G had understood the potential scale of break costs.

Lloyds is correct that in 2012 there would have been only two years to run on a five-year cap taken in 2009. But by 2012 interest rates had been very low for four years, which I think would have influenced G's director's thinking about hedging. No one knew whether rates would stay low, but I think it's likely that G's director – especially in the light of his comments above about gambling – would have regarded the two years left on the cap as enough protection, with the intention of reviewing things when it expired.

For these reasons, I'm satisfied that replacing the fixed rate loan with a variable rate loan is a fair and reasonable outcome of G's complaint about the 2012 loan.

consequential losses

I need to look at whether the bank's failures actually caused the consequential losses claimed by G. And if they did, I also need to ask whether it's fair to hold the bank responsible for the losses. To do this, I'd need to ask whether the bank could reasonably foresee that its failures would result in losses like these. In other words, I'd need to be satisfied that the losses weren't too remote from the bank's failings.

Having considered all of G's points, I agree with the adjudicator's conclusions, largely for the reasons he gave. G suffered other business difficulties which were unrelated to the cost of the fixed rate loans. Even if his loans had been on variable rates, I don't think the savings would have been enough to avert the losses. I don't think the fixed rate loans were the cause of the losses listed by G.

I've read the recent letter from the potential investor but it doesn't change my view. Given the problems faced by G's business, I can't conclude that the proposed investment was more likely than not to have gone ahead in the absence of the fixed rate loans, or that the investment would have rescued G's situation in 2014. Moreover, it seems the potential break costs were mainly an obstacle to the investor's requirement for G to move its banking facilities, and I don't regard that requirement as something the bank ought to have foreseen. I think the argument about the proposed investment is too speculative and in any event the losses are too remote from the bank's failures, so I don't conclude that the bank is responsible for the losses.

I therefore don't make any award for consequential losses.

my final decision

My final decision is that I uphold G's complaint about the 2012 fixed rate loan. I require Lloyds Bank PLC to reimburse G as though the £101,500 loan taken in November 2012 was on a variable rate from the outset. The redress should reflect the following practical considerations:

- The bank should reimburse the difference in payments between the fixed rate loan and the variable rate loan, from the date the loan was taken to the date the account was transferred to the bank's recoveries department and loan payments suspended.

- Interest should be added at 8% simple from the date the costs were incurred to the date the account was transferred to the bank's recoveries department. If the bank believes it’s legally obliged to deduct tax from the interest, it should send the customer a tax deduction certificate.

- The bank should refund the break costs.

Under the rules of the Financial Ombudsman Service, I’m required to ask G to accept or reject my decision before 1 March 2018.

Colin Brown
ombudsman