

## **complaint**

Mr and Mrs M are business partners. They complain that Clydesdale Bank Plc mis-sold them a fixed rate loan and it hasn't offered to pay enough compensation.

## **background**

The circumstances leading to this complaint were set out in my provisional decision dated 25 January 2016, a copy of which is attached and forms part of my final decision.

In July 2008 Mr and Mrs M took out a £1,408,000 loan from Clydesdale Bank to refinance borrowing on their property portfolio. The partners agreed to fix the interest rate for the full 20-year term. The agreement was broken in late 2012 at a cost to the partners of £393,255. Shortly afterwards their property portfolio was sold.

Mr and Mrs M complained that the fixed rate loan was mis-sold and they suffered direct and consequential losses. In particular, they said the bank was responsible for losses resulting from the sale of their properties.

It was my view that Clydesdale should put the partners in the position they would have been in if they'd fixed the rate for only five years and on only half of the loan. I also thought the bank should pay them £750 compensation for the trouble and upset they suffered. For the reasons I explained in the provisional decision, I didn't think the bank needed to pay any compensation to the partners for consequential losses.

I asked the parties if they wanted to send me anything further in response to my findings.

Clydesdale said it disagreed that the rate should be fixed on only half the loan. It thought reducing of the term of the fixed rate from 20 years to 5 years – on 100% of the loan – would be a fair and reasonable outcome. It reiterated that the bank is entitled to use its own commercial discretion regarding the terms on which it will lend. But having said this, the bank was prepared to comply with my proposals to bring the matter to a conclusion.

Mr and Mrs M thought the provisional decision didn't propose enough compensation. Their representative said it shouldn't be based on a replacement loan with a fixed rate, and there should be substantial redress for consequential losses. The representative made the following points, among others:

- If the partners had fully understood the risk of break costs, they wouldn't have agreed to a fixed rate for any term. They would have either agreed a variable rate loan or declined to move their banking to Clydesdale.
- Fixing the interest rate was a condition of the loan. In an email before the loan was agreed, the bank said the loan must have full interest rate protection for the full term. It was never any option for the partners to fix on part of the loan, so to suggest that could have happened is completely artificial.
- Without the fixed rate, Mr and Mrs M wouldn't have breached the LTV covenant. So they wouldn't have had to sell the property portfolio.

- The LTV ratio was at the limit of the loan covenant from the start. No sound business adviser would recommend to a client to undertake such borrowing in those circumstances.
- Mr and Mrs M's consequential loss claim should be assessed on the basis that they wouldn't have had personal guarantee liabilities from their limited company's borrowing. The company wouldn't have taken on the lending if the directors had been fully informed, and there would have been no guarantees.

## **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've given careful thought to the representative's argument that the partners wouldn't have agreed to a fixed rate for any term if they'd been aware of the risk of break costs.

It isn't possible to be certain what would have happened, so I have to decide what was most likely. The loan was for 20 years, for a property portfolio. At the time Mr and Mrs M didn't intend to repay the principal in less than five years. In the circumstances, I think fixing the rate for five years would have seemed attractive to the partners. I also believe the fact they elected to fix the rate for 20 years shows they had some appetite for controlling their interest costs.

If they'd known the potential break cost risks, I'm sure they would have regarded a 20-year fix as too risky. But I believe they would have seen fixing for the first five years as a reasonable balance of benefit and risk – especially if it was only on half the loan. I conclude that, if properly informed, Mr and Mrs M would have been likely to agree a five-year fix.

I don't believe the loan agreement made fixing the interest rate a condition of lending. Mr and Mrs M's representative correctly says the bank proposed this in an email during the discussions before the loan. But I'm satisfied that in the end it wasn't a condition – it didn't appear in the agreement. This was in contrast to the loan agreement for the limited company, which did state that interest rate hedging was a condition.

Clydesdale believes there should be no adjustment of the replacement loan to take account of the LTV covenant, while Mr and Mrs M's representative feels the impact of the covenant was worse than I described. To the bank I can only repeat that although it was entitled to set the covenant, it added extra risk to the fixed rate loan by doing so. I still think that if Mr and Mrs M had been fully informed, they would have wanted more flexibility to manage that risk. I note that in the event the bank didn't act on the breach until the LTV had exceeded the covenant level for a year. Taking all the circumstances into account, I still think it's fair and reasonable to base compensation on fixing the rate on half the loan.

I'm sorry to say I can't examine the circumstances of the limited company's borrowing here. The current complaint is solely about the partnership's borrowing. The company's borrowing was the subject of a separate complaint which this service couldn't investigate because the company no longer exists.

I realise Mr and Mrs M will be deeply disappointed that I've made no award for consequential losses. But having looked again at all the evidence and arguments, I still think that even if they'd fixed the rate on only half of the loan and only for five years, they wouldn't have been

able to rescue their situation in 2012. So I can't say the bank's failings caused the property portfolio to be sold.

For these reasons, I don't depart from my provisional decision.

### **my final decision**

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.

#### *determination and award*

I uphold this complaint. I believe Clydesdale didn't provide Mr and Mrs M with information which was clear, fair and not misleading. I think Mr and Mrs M would have fixed their rate for five years on half their loan, instead of for 20 years on the whole loan, if they'd been given sufficient information.

I consider that fair compensation requires Clydesdale Bank Plc to carry out the steps I specify below. I order the bank to do this – up to a maximum financial effect of £150,000.

#### *recommendation*

If the financial effect of my award exceeds £150,000, I recommend that Clydesdale Bank Plc still carry out in full the steps I specify.

This recommendation doesn't form part of my determination or award. It doesn't bind the bank. It's unlikely that Mr and Mrs M could accept my decision and go to court to ask for the balance. They may want to consider getting independent legal advice before deciding whether to accept this decision.

#### *the specified steps*

Clydesdale Bank Plc should reimburse Mr and Mrs M as though they had agreed to fix the interest for five years on half their £1.408 million loan from the outset, with the other half of the loan on a variable rate. The award should reflect the following practical considerations:

- The bank should reimburse the difference between the break costs originally incurred and the break costs that would have been incurred on ending the replacement product at the same time.
- The bank should reimburse any difference in payments between the original and the replacement product up to the point when the fix was broken.
- Compensatory interest should be added at 8% simple per annum to the reimbursed payments from the date the cost arose to the date of settlement.
- The bank may use the financial compensation specified in the paragraphs above to offset any of Mr and Mrs M's existing debt to the bank and debt written off during these events.

- If Clydesdale believes it's legally obliged to deduct tax from any interest, it should send a tax deduction certificate with the payment.
- The bank should in addition pay Mr and Mrs M £750 compensation for trouble and upset.

For reasons I explained above, I make no additional award in respect of consequential losses.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr and Mrs M to accept or reject my decision before 11 April 2016.

Colin Brown  
**ombudsman**

## **COPY OF PROVISIONAL DECISION**

### **complaint**

Mr and Mrs M are business partners. They complain that Clydesdale Bank Plc mis-sold them a fixed rate loan and it hasn't offered to pay enough compensation.

### **background**

In July 2008 Mr and Mrs M took out a £1,408,000 loan with Clydesdale Bank to refinance borrowing on their property portfolio. It had a 20-year term and initially the partners would only pay interest instead of paying off the capital. The partners agreed to fix the interest rate for the full term.

The fix was broken in late 2012 at a cost of £393,255 to the partners. Shortly afterwards their property portfolio was sold.

Our adjudicator recommended that Clydesdale should put the partners in the position they would have been in had they fixed half of the loan for five years. He gave these reasons:

- The bank didn't do enough to explain how much it might cost to leave the arrangement early. The adjudicator believed the partners required a degree of flexibility, which the 20-year fix could severely limit. He thought that if they'd understood the risk of break costs, they'd have chosen a five-year fix.
- The loan contained a covenant under which the partners' property portfolio couldn't exceed a 55% loan to value ratio (LTV). At the time the partners were looking to take out the loan, the bank was aware that the intended borrowing had an LTV of 52%.
- Our adjudicator didn't question the bank's commercial judgment in setting the LTV covenant at 55%. But he thought that if the bank had properly explained the potential break costs, the partners wouldn't have fixed all of their borrowing. Given the tight LTV, this would have given them scope to repay the unfixed part of the loan – and so avoid the risk of break costs – if the value of their property portfolio dropped below the covenant's limits.

Clydesdale was content to shorten the term of the fix to five years. But it didn't agree that the fixed rate should be applied to only half of the loan.

Mr and Mrs M agreed with the basic redress recommended by the adjudicator. But they still wanted compensation for the consequential losses caused by the fixed rate loan. Specifically, their claim is for:

- the sale of their property portfolio
- the sale of personal items to cover living costs
- the impact on their health

### **my provisional findings**

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

*the mis-sale and the replacement product*

It's common ground that there should be a replacement product. I agree that the bank didn't properly explain the potential scale of the break costs. Compensation should be based on what Mr and Mrs M would've done if they'd been given enough information.

I've considered the issue of the appropriate replacement product. I think the adjudicator was right to conclude the partners would have fixed half the loan for five years.

As regards the LTV covenant, I agree that the terms on which Clydesdale offered lending were a matter for its commercial discretion. But I think the tight LTV covenant would have been an important additional risk factor for Mr and Mrs M if they'd understood the scale of potential break costs. As it was so close to the actual LTV from the start, there was a real risk that external events or moderate changes in the fortunes of their business would lead to a breach of the covenant and an early exit from the fix.

If the partners had fully understood how much an early exit would cost them, I don't believe they would have agreed to fixing on the whole loan. I agree with the adjudicator that leaving half the loan on a variable rate would have given Mr and Mrs M more flexibility. So I think that's what they would have agreed.

*consequential losses*

I need to look at whether the bank's failures actually caused consequential losses for the partners. 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 the losses weren't too remote from the bank's failings.

In making these assessments, I need to compare what actually happened with what's likely to have happened if Mr and Mrs M had the replacement product. So the comparison is between events under the 20-year fix for the whole loan and likely events under the five-year fix for half the loan.

*the sale of the property portfolio – did the fixed rate loan cause losses for the partners?*

The partners say the fixed rate loan caused them to sell their property portfolio.

In October 2011 the bank realised the partners had breached the 55% LTV covenant. The bank gave the partners a year to repair the breach but in October 2012, with the partners' borrowing now at an LTV of 63.6%, the bank called in the lending.

The bank says that, to repair the covenant breach, the partners would have had to reduce their borrowing by £187,000.

In considering whether the partners would have had resources to repair the covenant breach, I need to take into account their wider financial circumstances. Mr and Mrs M also had a company, which ran a hotel business. The company was in financial difficulties, and the bank was asking Mr and Mrs M to pay the £260,000 personal guarantee they'd pledged to support it.

Taking all this into account, I believe that by 2012 Mr and Mrs M didn't have enough financial reserves to rescue their situation. The only assets they had left were tied up in their property portfolio. I can't see how they could have moved forwards without selling their properties. Selling only part of the portfolio wouldn't have been enough to repair the LTV and meet their other urgent commitments.

For these reasons I conclude that, even if Mr and Mrs M had only hedged half of the loan amount for five years, they'd still have had to sell their property portfolio. So I can't say the bank's failings caused the property portfolio to be sold.

Because I don't think the lost profits were caused by the bank's actions, I don't need to determine whether they were foreseeable.

*the sale of personal items to cover living costs - did the fixed rate loan cause losses for the partners?*

Mr and Mrs M say they had to sell personal items to stay afloat. But I've already concluded they would have been in financial difficulties even with the replacement product. So I can't say the bank's sale of the original product caused their losses.

I'm sympathetic to the partners' difficulties. If the assumptions I've made are wrong, I'll reconsider the claim. If that's the case, the partners should provide detailed evidence of what items were sold and how the losses have been calculated.

*the impact on Mr and Mrs M's health – did the fixed rate loan cause the losses?*

Mr and Mrs M have had financial difficulties and suffered from serious health problems. They have been through a wretched time. But I've already said they would have been in financial difficulties even with the replacement product, so don't think it's possible to say the sale of the original product was the cause of their other troubles.

Having said that, I believe it's likely that the worry and disruption caused by having the longer fix for the higher amount made things worse for Mr and Mrs M at an already difficult time. So in addition to the compensation for financial loss, I'm minded to make an award for trouble and upset. I think it would be fair and reasonable for the bank to pay £750 compensation for this.

### **my provisional decision**

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.

### *determination and award*

I'm minded to uphold this complaint. I believe Clydesdale didn't provide Mr and Mrs M with information which was clear, fair and not misleading. I think Mr and Mrs M would have fixed their rate for five years on half their loan, instead of for 20 years on the whole loan, if they'd been given sufficient information.

I consider that fair compensation requires Clydesdale Bank Plc to carry out the steps I specify below. I provisionally order the bank to do this - up to a maximum financial effect of £150,000.

### *recommendation*

If the financial effect of my award exceeds £150,000, I may recommend that Clydesdale Bank Plc still carry out in full the steps I specify.

This recommendation wouldn't be part of my determination or award. It wouldn't bind the bank. It's unlikely that Mr and Mrs M could accept my decision and go to court to ask for the balance. They may want to consider getting independent legal advice before deciding whether to accept this decision.

### *the specified steps*

Clydesdale Bank Plc should reimburse Mr and Mrs M as though they had agreed to fix the interest for five years on half their £1.408 million loan from the outset, with the other half of the loan on a variable rate. The award should reflect the following practical considerations:

- The bank should reimburse the difference between the break costs originally incurred and the break costs that would have been incurred on ending the replacement product at the same time.
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- The bank may use the financial compensation specified in the paragraphs above to offset any of Mr and Mrs M's existing debt and debt written off during these events.
- If Clydesdale believes it's legally obliged to deduct tax from any interest, it should send a tax deduction certificate with the payment.
- The bank should in addition pay Mr and Mrs M £750 compensation for trouble and upset.

For reasons I explained above, I'm not minded to make any additional award in respect of consequential losses.

Colin Brown  
**ombudsman**