FINAL DECISION	
complaint by:	the W Family
complaint about:	Bank E
complaint reference:	
date of decision:	July 2013

This final decision is issued by me, Tony Boorman, an ombudsman with the Financial Ombudsman Service. It sets out my conclusions on the dispute between a family business – the W Family – and Bank E about an interest rate hedging product – a swap.

Under the rules of the Financial Ombudsman Service, I am required to ask the W family to let me know whether they accept or reject my decision by 27 September 2013.

summary of complaint

This dispute is about the sale by Bank E to the W Family business of an interest rate hedging product – a "swap" – with reference to a loan agreed by Bank E. The sale took place in 2007.

my provisional decision

On 22 October 2012 I issued a provisional decision upholding this complaint. I provisionally concluded that in the circumstances of this case the "multi-callable swap" should not have been recommended to the W Family by Bank E – and the bank should have provided better information about the product it sold.

I invited the parties to reach a mutually acceptable agreement about a settlement in light of my initial observations. To help guide discussions, I set out what I considered fair compensation might look like in the circumstances. This was a replacement of the existing 15 year swap with one that would have allowed the W Family to exit the agreement at no cost after two years, albeit at a higher rate.

Representatives of the W Family proposed redress to Bank E based on breaking the swap immediately at no cost and refunding all payments the W Family had made under the swap, with interest. The proposal also included a payment for 'reasonable costs' which the W Family said it incurred, in the shape of professional fees.

It does not appear that the W Family received a substantive response from Bank E, though both parties did agree to suspend all payments related to the swap until an agreement on redress was reached. The W Family also agreed that if Bank E accepted liability (i.e. that there was a mis-sale), they would allow the bank some time to agree to the redress proposal their representatives had provided.

Bank E wrote to me on 14 December 2012 and accepted my provisional decision regarding liability – i.e. that there was a mis-sale. However, it raised considerations about fair compensation, which I summarise as follows:

- As the W Family was under the impression hedging was a condition of the loan, it would have hedged for much longer than two years (particularly as one of the objectives of the company was to obtain a discount on the interest rate for the first two years and there was a long-dated loan).

- The W Family was not averse to making long term commitments. The loan was for nearly 15 years and the W Family did not seem to dispute it knew the swap matured after 15 years.

- The “multi-callable” feature of the swap did not necessarily mean the product was unfair. A rate lower than a non-callable swap was guaranteed for the first two years and the rate which would continue if the bank did not call the swap was lower than the rate available if the multi-callable feature was not present.

- The W Family was aware of the possibility of break costs. Though the bank could have provided the W Family with more information on the potential amount before 2009, this may not have impacted the decision to hedge – many customers did not foresee interest rates could reach the low levels they have. The bank would not consider compensation to be fair without appropriate breach costs liability on the part of the company.

Disappointingly Bank E did not engage in any material discussions with the W Family directly to allow the parties to come to a mutually acceptable agreement on the matter. The W Family did not agree to Bank E’s request for further extensions.

I wrote to both parties on 21 February 2013 to clarify my view on redress, which I will return to later. I noted that in the absence of any further submissions from the parties, in my final decision I was likely to order that Bank E reconstruct the W Family’s accounts as though a two year swap at the higher rate of 5.95% (rather than the initial discount rate of 4.38%) had been in place from the outset.

The W Family responded and requested that I reconsider my provisional decision that I should not make an award to cover the professional costs they incurred in pursuing this matter. This is in light of what the W Family considers the exceptional circumstances of the case.

In the meantime, Bank E has informed me it has calculated the redress the W Family may receive according to the methodology agreed with the regulator as part of the regulatory review of this sale. I will return to this later as well.

I have carefully considered the points made by both parties. Having done so, I am not persuaded that I should depart substantially from the findings set out in my provisional decision and subsequent letter of clarification.

background to complaint

a) events leading up to the complaint

The W Family run a small hotel business. In 2007 they decided to expand their business by selling one of the two hotels they ran and purchasing a new slightly larger hotel.

The family approached their bank for assistance. In early 2007 the family discussed with Bank E a business loan to purchase the new hotel (initially the loan was to be for £4.2m but decreasing almost immediately to approximately £2.2m once the “old” hotel had been sold).

In assessing the loan, Bank E's relationship director noted in an internal memo that the W Family's bank accounts had been run in "*an exemplary fashion*" and the account was "*very low risk*". The relationship director concluded that there was a "*clear cut opportunity to lend*" to the W Family "*who have been very cautious and prudent in their timing to expand*".

The loan was in due course approved on the basis of a variable interest rate of Bank E's Base + 1.25% repayable over a 14 year term. At around the same time there was a discussion of a "callable interest rate swap". The precise nature of this arrangement I will set out in more detail later in this decision. But in essence it was a separate agreement with the bank under which any variation in the loan interest rate-payable was netted off against payments to or from the bank – with the overall impact that the loan rate became fixed. The swap was established for a period of 15 years, with an initial two year discounted rate.

In 2009 there was a further discussion between the family and Bank E. The initial discount rate under the swap was due to come to an end and the net effective pay rate increased from 4.38% to 5.95%. The covenants and security surrounding the loan were re-arranged and a new loan agreed. At this time the family had also discussed with Bank E the possibility of terminating the swap agreement. They were told that at that time the charge for breaking the swap would be around £542,000, a sum they could not afford.

Subsequently Bank E and the family have continued a dialogue about the accounts, loan and the swap. In 2011 the bank suggested a number of possible changes which involved amongst other things a new loan to meet the then break costs of the swap of around £550,000.

The family has become increasingly concerned by the burden that the swap now represents on their business, which trades profitably but like many other businesses is under pressure given wider market difficulties.

b) The complaint and the bank's response

Relations between the bank and the family declined and the family raised a formal complaint about the swap and associated arrangements. They said:

- the bank suggested a transaction that was not in the company's best interests; and
- the implications of the swap were not fully explained

Bank E did not agree. It said it was satisfied that it had acted appropriately and that the decision to enter the swap was one that the family had freely made on their own risk without formal advice from the bank.

The W Family were not satisfied by this response and they referred this complaint to the Financial Ombudsman Service.

The complaint was investigated by one of our adjudicators who obtained further information from the parties. The adjudicator's opinion was that the complaint should not be upheld. The W Family objected to that initial assessment and reiterated their concerns about the swap. As the parties could not agree on an outcome – and in view of the significance of the sums involved and the wider interest in disputes of this nature – the dispute has been referred to me for determination under the rules of the ombudsman scheme.

Accordingly, in light of these developments and given the desirability of resolving matters as promptly as practicable – while recognising the significance of the issues for both parties – I issued my provisional decision on this case.

my findings

I have included only a brief summary of the complaint (above), but I have read and considered all the evidence and arguments available to me from the outset, (including the further submissions made following my provisional decision) in order to decide what is fair and reasonable in all the circumstances of this complaint.

a) jurisdiction

I do not have a free hand to investigate complaints from all of Bank E's business customers. I can only consider complaints from those businesses and other customers who meet the eligibility criteria set out in the dispute resolution rules (DISP) section of the Financial Conduct Authority's (FCA) Handbook of rules and guidance[1].

I am satisfied that the W Family business falls within my jurisdiction as it is a micro-enterprise – and as such it is an eligible complainant for the purposes of DISP. Broadly this means that, at the time the W Family business referred their complaint to Bank E, it was an enterprise which both employed fewer than ten persons and had a turnover or annual balance sheet that did not exceed €2 million.

In this context, in accordance with European Law, the number of 'employees' is calculated on a full time equivalent basis and includes: persons working for the enterprise being subordinated to it and considered to be employees under national law, owner-managers, and partners engaged in a regular activity in the enterprise and benefiting from financial advantages from the enterprise.

In this case the W Family business's annual turnover at the relevant time was slightly more than £500,000 and it had at most nine "employees", including all the family members who were involved. While this might seem a relatively small number of staff to run a hotel, I note much of the work at the hotel, including the cleaning work, was done by external contractors whose staff were not employees of the W Family business.

I am also satisfied that the W Family was, in the language of the FCA's recent statement on interest rate hedging products, a "non-sophisticated customer".

b) relevant considerations

When considering what is fair and reasonable, I am required to take into account relevant: law and regulations; regulator's rules, guidance and standards, and codes of practice; and, where appropriate, what I consider to have been good industry practice at the time.

I am mindful that this is a complaint between a relatively modest sized business customer and a bank. My general approach when considering cases in respect of business customers is to analyse the circumstances of the customer and the nature of the transaction. In broad terms the larger and more significant the transaction is, the more I would expect a business customer to pay particularly careful regard to its contents.

[1] The Financial Services Authority (FSA) at the time of this complaint was referred to me.

Similarly, the professional knowledge of the business and/or its ability to access professional support will be of relevance in assessing the case. A small corner shop for example, is unlikely to have the facilities to analyse complex legal and financial transactions and may be unable to access independent advice on the issues – whereas a larger business is more likely to have these facilities, or the ability to access independent advice.

So, depending upon the nature of the business, I might consider it fair for the bank to exercise more care in its dealing with the corner shop than with a large business. This might include going to greater lengths to make sure the business understands all the implications of the transaction.

I am also mindful that the protections available for personal customers (in law and in self regulatory codes) go beyond those made available to business customers in some respects. It is important therefore to avoid applying to this case (and similar cases) provisions and considerations that are only appropriate in the case of personal customers.

But this does not mean that business customers have no protection in law. Even if the complainant is not a *"private person"* under section 150 of the Financial Services and Markets Act 2000 (and therefore does not have a statutory right of action), that does not mean that the FSA Principles and Conduct of Business Sourcebook ("COBS") rules do not apply to the respondent business.

Neither does it mean that the Principles and COBS are irrelevant for the purposes of determining this complaint by reference to what is, in my opinion, fair and reasonable in all the circumstances. Clearly the same points can be made in respect of the Conduct of Business (COB) rules which preceded the present COBS and were in place when this swap was sold.

The application of many of the FSA rules at the time depended on the classification of the person with whom the financial business conducted investment business. In the Principles and COB, the term "customer" usually refers to a private customer and intermediate customer, but not market counterparties. The term "client" covers customers and market counterparties.

I am satisfied that for the purposes of the FSA rules at the time of the transaction, the W Family business was a "private customer", that is someone who is neither a "market counterparty" nor an "intermediate customer".

In other words, the W family was a private customer because it was it was not: a listed company, partnership with net assets of at least £5 million at any point in the previous two years, someone Bank E had classified as an expert private customer and taken the steps set out under COB 4.1.9R, or any of the other market counterparty or intermediate customer classes.

The Principles and conduct rules remain important standards that a financial business must still observe in the conduct of its business, irrespective of whether its customers are individuals or businesses, large or small. Many of those standards reflect the obligations that I would expect to exist at law anyway for a business in dealing with its customers.

In *R(BBA) v FSA and FOS* [2011] EWHC 999 (Admin) at 162, Ouseley J made it clear that the Principles are best understood as *'the ever present substrata'* which *'always have to be* *complied with'*. The Principles and more detailed conduct of business rules are therefore relevant considerations that I am obliged to take into account when considering what is fair and reasonable, in accordance with my obligations under DISP 3.6.4R and statute.

The Principles that are of particular relevance to this and other similar complaints are:

- Principle 1
  "A firm must conduct its business with integrity"

- Principle 6
  "*A firm must pay due regard to the interests of its customers and treat them fairly*"

- Principle 7
  "*A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading*"

- Principle 9
  "A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment".

In addition, in specified circumstances, the more detailed FSA's Conduct of Business (COB) rules apply. These came into force on 1 December 2001. Of particular relevance to this complaint are:

- clear, fair and not misleading communication

  COB 2.1.3R (from 1 December 2001)
  "When a firm communicates information to a customer, the firm must take reasonable steps to communicate in a way which is clear, fair and not misleading".

  COB 2.1.4G (from 1 December 2001)
  "When considering the requirements of COB 2.1.3 R, a firm should have regard to the customer's knowledge of the designated investment business to which the information relates".

- requirement to know your customer

  COB 5.2.5R (from 1 December 2001)
  "Before a firm gives a personal recommendation concerning a designated investment to a private customer, or acts as an investment manager for a private customer, it must take reasonable steps to ensure that it is in possession of sufficient personal and financial information about that customer relevant to the services that the firm has agreed to provide".

  COB 5.2.7G (from 1 December 2001)
  "If a private customer declines to provide relevant personal and financial information, a firm should not proceed to provide the services described in COB 5.2.5R without promptly advising that customer that the lack of such information may affect adversely the quality of the services which it can provide. The firm should consider sending written confirmation of that advice".

- requirement for suitability generally

  COB 5.3.5R (from 6 April 2006)
  "(1) A firm must take reasonable steps to ensure that, if in the course of designated investment business:

  (a) it makes any personal recommendation to a private customer to:

  (i) buy, sell, subscribe for or underwrite a designated investment (or to exercise any right conferred by such an investment to do so); or
  (ii) elect to make income withdrawals,

  …the advice on investments or transaction is suitable for the client.

  (3) In making the recommendation or effecting the transaction in (1), the firm must have regard to:

  (a) the facts disclosed by the client; and
  (b) other relevant facts about the client of which the firm is, or reasonably should be, aware".

- customers' understanding of risk

  COB 5.4.3R (from 15 November 2001)
  "A firm must not:
  (1) make a personal recommendation of a transaction;…
  with, to or for a private customer unless it has taken reasonable steps to ensure that the private customer understands the nature of the risks involved".

c) overview

Taking these considerations into account together with the points raised by the parties in this dispute, the key initial questions I need to ask are:

- whether Bank E gave the W Family advice about the interest rate swap (and if so whether the Bank took adequate steps to ensure that the advice was suitable); and

- if Bank E did not give advice, whether it gave the W Family information that was clear, fair and not misleading in order to put them into a position where they could make an informed choice about the swap.

d) developments since my provisional decision

i) legal issues

I am aware that since I issued my provisional decision, the Mercantile Court of the Manchester District Registry handed down its judgment in *Green and Rowley v Royal Bank of Scotland plc* [2012] EWHC 3661 (QB) – relating to an interest rate hedging instrument. The Court made some comments on the relevant legal and regulatory position. I have considered the judgment carefully. Having done so I am not persuaded there is a need to change the key questions outlined above or my approach to answering them.

The Court addressed issues concerning common law duties of care and *Hedley Byrne* negligent mis-statement (which establishes a duty of care owed in circumstances where a statement is made and there is reliance on it). The Court considered whether or not advice was given and if so, whether that advice was in breach. Briefly, in that case, which concerned a meeting which took place in 2005, the Court concluded that:

- It was difficult to retrieve evidence of the meeting between the parties in 2005. Green and Rowley's testimonies needed to be assessed alongside the evidence produced by RBS. The Court found RBS's evidence of the meeting to be impressive and reliable, as opposed to Green and Rowley's which was considered to be inconsistent.

- There was not enough evidence to suggest that advice was given in this case.

- The Court was not convinced that even if RBS had given certain details of the swap (relating to *'breakage costs'* and whether the swap was separate to the loan), Green and Rowley would not have proceeded. The Court did not consider COB 2.1.3R and 5.4.3R to be relevant to the duty not to make a negligent mis-statement, and in the event they did apply, there was no breach.

- In 2005, the margin had consistently been fixed for as long as the RBS representative could recall and therefore any change could not be envisaged.

- As the swap was, in principle, *'portable'* there could have been no mis-statement: Green and Rowley understood that any transfer to another bank would require that bank's consent.

I accept that the Court's decision in *Green and Rowley* is relevant to my considerations here and I have taken it into account. I am, however, mindful of the Court's finding that it was a *'highly fact-sensitive case'*.

In my opinion, the Family's complaint has a materially different factual matrix. Amongst other things, the Court found Green and Rowley to be *'both intelligent and experienced businessmen albeit not previously versed in swaps but this particular swap was very straightforward and they would have had no difficulty in understanding it, or if they did they would have asked.'* I have found the particular swap in the Family's complaint to be complex and that the Family had limited experience and access to professional advice.

I also note that the Court appeared to have found that COB 2.1.3R and COB 5.4.3R are not encompassed within the *Hedley Byrne* duty. This issue is not strictly relevant in the context of this decision (because I have found that advice was given). But even if this was a complaint solely about the provision of information, I would still consider the COB rules to be a relevant consideration that I would take into account, in accordance with my duties under DISP 3.6.4R and statute. That is because, as I have already mentioned, the Principles and the COB rules remain important standards that a financial business must still observe in the conduct of its business.

The Court's analysis in *Green and Rowley* was focussed upon the application of common law duties, rather than a direct analysis of the bank's adherence to the COB rules and other regulatory rules. Importantly, the judgment was not an assessment of what is fair and reasonable. I must determine this complaint by reference to what is, in my opinion, fair and reasonable in all the circumstances of the case.

I also note that, following an application for permission being granted, the Court's judgment in *Green and Rowley* is being challenged in the Court of Appeal.

ii) the regulator's statement

Since my provisional decision the FCA (at the time, the FSA) published its statement on the review of cases it had asked certain banks to carry out January 2013. It reported on the pilot findings and – in the words of its press statement – confirmed the start of a full review of interest rate mis-selling.

I have carefully considered the FCA statement. It is important to note that the statement deals with the arrangement for a proactive review of interest rate sales by certain banks. It is not directly concerned with how individual disputes should be handled. But both are concerned with delivering fair and reasonable outcomes – so the FCA's conclusions are, it seems to me, of relevance here.

I note the FCA stresses that '*to determine whether a sale complied with regulatory requirements, and if not whether redress is due, a case by case assessment of all relevant evidence is necessary*'. The FCA's analysis of the merits of these issues is, in my view, entirely consistent with the analysis I set out above. I note in particular the significance of clear disclosures generally, with a special focus on break costs, is stressed by the FCA, as is the importance of suitable advice.

In summary, nothing in the FCA statement gives me reason to change my analysis of the merits of this dispute. In my view, the review process described by the FCA and my decision here would seem based on similar broad principles.

On the specifics of redress it also appears to me that the FCA principles for the review and my proposed approach in this case are aligned. My conclusion on redress here is specific to the particular circumstances of this case, but also seems consistent with the alternative product provision in the FCA approach.

e) summary

I have reconsidered these issues in the light of the representations of the parties and the other relevant developments I highlight above. I am satisfied that for the purposes of resolving this dispute the key initial questions I need to resolve remain those set out in the overview above.

To explore these questions I need to consider the terms of the swap (and associated agreements) and the way it works in practice and how the various arrangements were agreed (the transaction process).

about the initial arrangement

Interest rate swaps take various forms and the issues associated with each are somewhat different. This swap was an agreement separate from the loan agreement and entered into by the W Family and Bank E (albeit a different trading division of the bank from that which agreed the loan itself).

As such it was an investment product that, while connected to the loan, was separate from it. In this case, unlike in some other swaps, the swap was required to be terminated if the related loan was settled (albeit with any relevant fees). In practice it seems that this provision was not applied as the swap was not terminated when the new loan was agreed in 2009.

The particular swap in this case was described as a "multi-callable interest rate swap". The swap was set to cover a sum of £2m and had a 15 year term. The swap provided a means by which net payments were fixed for two years so that the effective rate payable was 4.38% – the 'discounted rate' period.

The swap provided for a higher fixed rate of 5.95% after the "first call" (the two year anniversary of the start of the swap when the discounted period ended) that would last for the remaining 13 years of the swap. Subject to any difference between LIBOR and base rate the effective pay rate for the customer was then 1.25% (the "margin" required over base rate by the Bank E in the loan agreement) over these swap figures – so initially the Family would effectively pay 5.63%.

To set these rates in context, it is worth remembering that at the time of this transaction base rate was 5.75% – so the pay rate under the loan was expected to be 7%.

Clearly a fixed rate arrangement has, in principle, a number of attractions for the parties. The borrower knows the maximum amount of interest they will need to pay, regardless of base rate fluctuations. And the lender has some additional assurance that the borrower will be able to service the debt in a range of interest rate environments.

However, in fact this swap only provided limited protection for the borrower. That is because after the first call (the second anniversary of the deal) the bank had the option to terminate the swap agreement for any reason – after which the consumer's position would be unhedged. Indeed, the bank noted that in the event that market rates were above the swap fixed rate it could terminate the agreement without (much) notice and without any compensatory payment to the consumer. That was not just an option the bank had on the first call date, but one which it retained to itself each and every month throughout the rest of the 13 years.

But this was not an option available to the consumer. Here the W Family could terminate the swap on notice, but only with what the bank described as "an economic cost to terminate". In practice that meant a calculation by the bank of the loss or profit to itself of the agreement being terminated. This would be determined largely by market conditions at the time – not some predetermined formula.

In essence, as I understand the position, if the expected future path of interest rates at the point of termination was expected by the market to be *above* the hedge position, the bank would make a gain (as it could sell the outstanding position in the market). Conversely, if the market expectation was for rates *below* the hedge rate then the bank would make a loss (it would forego the expected margin or incur costs in the market to net out its position).

Of course in the former case (where rates were, and were expected to remain, above the fixed rate) the bank would after two years be able to terminate the rate – so the possibility of a substantial benefit being paid to the consumer in the real world is perhaps questionable.

If market sentiment remained reasonably constant from the outset, then the costs of termination would be (relatively) modest. However, in such cases it is likely that the swap will achieve little for the parties – other than to smooth out relatively modest variations in interest rates. But the sums involved can be substantial if the expectation of future rates is significantly different from the position established in a swap.

To give a very simplistic example: a variation of 3% in rates for a £2m loan equates to about £60,000 a year in interest. Again, simplistically, if that differential was expected to exist over the next ten years of the loan then the “economic cost” of termination could it appears amount to well over £500,000 (note that is around a quarter of the value of the loan itself).

Another feature of this swap that is worth noting is that it tied the rate calculations to one month LIBOR, not to Bank E’s base rate (or Bank of England base rate) that the loan itself was based on. The bank presented this as a selling point as LIBOR was (it said) usually higher than Base Rate.

Furthermore, the swap was for the full £2m throughout the 15 years – it did not amortise (reduce in line with the planned repayments of capital) even though it was expected that the W Family would start making capital repayments against the loan after the first two years. It also lasted for a year longer than the loan itself. This meant that the swap would expose the family in later years to an investment risk – associated with market interest rates – significantly greater than was required to hedge the risks arising from lending in later years of the loan.

So, to summarise the swap, it provided the bank with a valuable safeguard that – so long as it decided to retain the swap – the family was protected from adverse interest rate movements that might put in doubt their ability to service the loan. For the family, the swap provided a useful discounted interest rate period. And, if market rates remained around or about the levels in the swap, it provided a useful way of smoothing out year-to-year volatility in rates (the impact of which on a small business could be significant).

However, if rates moved significantly and consistently *away* from the rate set in the swap, it provided questionable benefit to the family and – in certain circumstances – would act as a major restriction. That is because if rates increased (and especially if they were expected to remain high) the bank had the ability to terminate the deal at any time after the first two years, leaving the family unprotected from the higher rates.

In contrast, if rates fell significantly and consistently (as has been the case) then the family would (under the swap) pay rates above market rates and would not be able to terminate the agreement without a very substantial fee.

The net effect of all this is that outside a relatively narrow rate margin, this particular swap represented a one sided deal. If rates *rose*, the bank would not lose (because it could terminate the deal). If rates *fell*, the bank would not lose either (as the family would be effectively tied in to the life of the deal through cancellation fees). In this way, under the guise of a rate-fixing agreement, the risk of rates varying significantly from the then expected future path of interest rates was effectively transferred back from the bank to its customer.

But it should be noted that customers normally carry all interest rate risk if they have a variable-rate loan. The swap provided some benefit in terms of smoothing out year-to-year fluctuations. And there is nothing objectionable about fixed rate loans with (to borrow language from the retail sector) reasonable extended “tie-ins” and/or “redemption charges”.

Just as with many loans today, consumers may be paying a rate that is above current prevailing market rates – if they 'fixed' at a time when rates were expected to remain high. That will be disappointing for the consumer – but the lender will have done nothing wrong if the consumer freely chose that deal with good information about the terms that would apply.

about the transaction

The first record I have seen of a discussion is in an internal Bank E record dated 1 May 2007 produced by the relationship director. This is clearly a record of an earlier conversation with the family, and described the proposed hotel purchase and associated financial arrangements from the bank's perspective.

It concluded *"I would certainly recommend sanction, with hedging to be a condition for at least 50% of the loan"*. There is some uncertainty about interpretation here. The "loan" in question was then planned for £4.2m although this was to be rapidly offset by the expected proceeds of the sale of the "old" hotel. So it is unclear if 50% referred to £4.2m or the net £2.2m.

By mid June 2007 contracts were exchanged on the purchase of the "new" hotel. In early July a meeting was held between the bank and the family to finalise the financing arrangements. The family say that the bank told them that the loan would not pass credit control without a swap agreement in place.

The bank's representative from its corporate division (that was responsible for the swap transaction) was present at the meeting. According to the W Family, he said that interest rates were more likely to go up than down, that the swap could be renegotiated in three years, and that the initial discount rate version of the product best met the family's needs.

Bank E has no notes of the meeting available, but the next day it sent an email to the family. The email (11 July) said:

> *"Hi everyone,*
> *It was great to meet you yesterday and talk through the business, it certainly sounds like it is quite an exciting time for everyone!*
> *As I promised I have attached further details of the callable swap idea we went through yesterday…..*
> *Before we can put the Callable Swap in place we will require you to sign and return a FSA Risk Warning Notice. This is a standard document which covers a range of financial instruments……"*

The bank asks the family to fax back a signed copy of the Risk Warning Notice which was found *"in the appendix of our Terms of Business (also attached)"*

Attached to the email were two documents, a personalised document purporting to explain the Callable Swap and the bank's terms of business.

The swap Illustration has three pages of text and says:

> *"You can fix your interest rate costs on a notional amount of borrowing by entering Interest Rate Swap (sic). In this way, you would be completely insulated against increases in Base Rate and have certainty vis a vis repayments"*.

The document then describes a fixed rate product with an illustrative rate of 5.89%. In reference to this arrangement the document notes:

> *"The structure would fully protect you against a rise in interest rates above 5.89%, but you would not be able to benefit from any fall in rates below 5.89%"*.

The document then describes the "multi-callable interest rate swap" (the product variant the family agreed to purchase). The document says:

> *"There is an initial term of the Callable Swap, prior to the Call date where you have a known discounted Swap rate. At the Call Date and each month thereafter [Bank E] has the right to terminate the remainder of the structure or not. If the Bank elects to terminate, then you revert to being unhedged"*.

The document sets out three variants (with slight differences in the initial discounted rate and subsequent rates). It seems the previous discussion had focused on one of these options. The option for an initial discounted rate of 4.38% reverting to 5.95% is then explained, by reference to positive and negative interest rate movements within the initial discount period.

The section concludes:

> "*There is no up-front premium payable for this structure. However, if for some reason you decide to cancel the arrangement, you may face cancellation fees*".

The remainder of the document seeks to explain the issues surrounding "fixing against LIBOR and borrowing against base rate". The bank says:

> *"Fixing your interest costs against LIBOR generally works in your favour as long as LIBOR remains above Base rate (which it generally is as the UK high street banks are less creditworthy than the Bank of England itself!)"*.

The document does not specifically reference the length of the agreement, except in so far as each example table includes a swap starts date (July 2007) and a swap ends date (July 2022). The implication is that the length of the swap was never an issue in debate in the discussion – or if it was, then this had been resolved at the meeting.

The terms of business document is a complex document of 22 pages that sets out the general terms of business. It included at appendix 2 the "FSA Risk Warning Statement".

This statement says in the first paragraph:

> *"This notice cannot disclose all the risks and other significant aspects of derivative products such as futures, options, and contracts for differences. You should not deal in these products unless you understand their nature and the extent of your exposure to risk. You should be satisfied that the product is suitable for you in the light of your circumstances and financial positions".*

The family returned this document signed on the last page under the words:

> *"I/We confirm that I/We have received the General Terms of Business and hereby agreed to them and have read and understood the risk warnings set out above".*

I note the risk warning – to which the bank has referred in subsequent correspondence – does not refer to “swaps” and that the presentations made available to the family did not explain that the swap was a “derivative product”. I find it doubtful that the family fully understood how (if at all) this risk warning referred to their circumstances.

It is clear that the transaction was by then moving at an almost unstoppable pace. Contracts had been exchanged on the new hotel purchase and on 13 July the family returned to the bank the signed copy of the terms of business (and risk warning).

That afternoon the bank put in place the callable swap in a telephone conversation with the family. The call recording is brief and focused on confirming the details of the transaction. The family ask for confirmation that the deal is the best thing the bank has. The bank’s representative notes as part of the wider brief product description, that there may be a break cost or benefit. But he does not explain how this will be calculated.

At the close of the day on 13 July the bank sent the family an email letter describing the swap. This largely confirmed the details previously noted in the document attached to the email two days previously, but the “callable interest rate swap” is now described under the heading “agreed strategy”.

As can be seen, the transaction was carried out in a rush (as many of these transactions are). The first meeting about the swap took place on 10 July and it was transacted on 13 July. The W Family were in a rush to complete their hotel purchase and seemed to pay relatively little attention to the details of the transaction. But the bank too was in a rush. And the bank took what might be described as a relaxed attitude to the paperwork underpinning the loan and swap agreement – the key documents were all sent and signed after the transactions had taken place.

On the Monday (16 July) the Bank confirmed the rate and details of the swap it had agreed. That letter:

- confirmed the details of the swap rates; *and*

- emphasised the bank’s option to terminate the agreement at the end of the first call and thereafter.

But the letter was confused on a further point. At one point it required the family to agree (under the heading “non-reliance”) that:

> *“it has made its own independent decisions to enter this Transaction and as to whether the Transaction is appropriate or proper for it based on its own judgement and upon advice from such advisors as it has deemed necessary. It is not relying on any communication (whether written or oral) of the other party as investment advice or as a recommendation to enter into this transaction;….”*

And (under the heading *“assessment and understanding”*)

> *“Each party represents to the other party that it is capable of assessing the merits and understanding (on its own behalf of through independent professional advice), and understands and accepts the terms, conditions, and risks of this transaction….”*

However the letter also provided for advised sales. It says "*if you are a private or intermediate customer we may have agreed to provide you with advice…*". In these cases the provisions on non-reliance and assessment and understanding are not to apply. The letter is silent on whether or not Bank E did, in fact, believe that advice was provided to the W Family.

The rest of the paperwork was not tidied up for some time after the transaction. The loan agreement was eventually sent to the family on 27 July for signature. It is relevant to note that while this included various conditions – including those relating to security – it did not include any requirement on the family to enter into the interest rate swap, despite the family's clear recollection that it had been presented as a *requirement* while the transaction was taking place.

On 31 July the bank eventually sent the "treasury master agreement" which governed the operation of the swap. This agreement was endorsed (retrospectively) by the family at a board meeting in August 2007, when the family board noted the transaction "*would achieve the Company's aim of hedging the effect that changes in interest rate may have on its business"*.

The treasury master agreement is seven pages long. It sets out the general terms of the swap transaction. Of particular relevance to this dispute are the sections on representations and how the swap would operate in the event of early termination by either party.

The section on representations includes provisions which mimic the "non-reliance" and "assessment and understanding" provisions in the letter of 13 July (no mention is made here of advice from the Bank).

On termination the agreement primarily provides for acts of default (for example, where there is a default on payments against the underlying loan). There are no explicit provisions governing the circumstances where a customer wishes to terminate the swap early.

But by inference from the terms relating to non-payment of amounts due under the swap or of early settlement of the loan, the party terminating the swap has to indemnify the other for any costs it incurs. These are defined to include:

> *"any loss of bargain, costs of funding or any loss or costs incurred as a result of terminating, liquidating, obtaining or re-establishing any hedge or related trading position"*.

The agreement covers the circumstances where this might represent a "gain" as well as a loss. But it is up to the non-defaulting party to calculate the "loss". So where the consumer seeks to terminate the agreement, the bank calculates its own loss against, amongst other things, its own trading position. And subject to "*showing such calculations in reasonable detail and including all relevant quotations*" the loss so calculated is binding on the consumer.

my conclusions on key issues

Accordingly, my conclusions on the key initial questions I need to answer are set out below:

- whether Bank E gave the W Family advice about the interest rate swap, *and if so,* whether the bank took adequate steps to ensure that the advice was suitable for the W Family.

The documentation is unclear and contradictory about whether or not advice was given. The treasury master agreement requires that it was not, but other documentation is ambiguous.

The notion that the family should obtain its own financial advice before agreeing the swap was not highlighted and the bank knew that the advice and support available to the family (other than that provided by Bank E itself) was limited. The W Family, while business people, were not knowledgeable about financial transactions of this nature. Accordingly, it was not credible in my view that the family could represent that they were capable of understanding and accepting the terms and risks of the swap.

Rather, the Bank introduced and explained the notion of the swap. It clearly took the family through some options and produced a note that described the determined outcome as “the agreed strategy”. It did not, to my mind, make clear that it was not giving advice – rather it encouraged the family during this rushed transaction to rely on its advice and recommendations.

Certainly it will have appeared as advice from the family’s perspective. The bank directed the family to this product, selected the term over which it was to operate and actively encouraged (perhaps to the point of making it a requirement) the purchase of the swap.

I therefore conclude that in the circumstances of this case – despite the lack of a clear confirmatory statement at the time by the bank – the actions of the bank did, in fact, amount to professional investment advice in relation to the purchase of this swap. It should, therefore, have followed the obligations in respect of suitability and other matters that regulation (and the law) place on an investment advisor in such a transaction.

In my view, the advice that Bank E gave paid insufficient attention to the needs of the W Family. The swap was a poor fit for the circumstances of the family. While it provided worthwhile protection in certain circumstances, and a valuable initial discount, it also provided little long term protection from rising rates. But it could, in very low interest periods, effectively tie in the family to the arrangement because of exceptionally high cancellation charges.

Bank E has said in response to my provisional decision the “multi-callable” feature of the swap alone does not make the product unfair. It emphasises that the W Family received a discount in the rate for at least two years through this structure, and possibly longer if the bank did not cancel the product. I recognise the rate for a shorter-term swap would have been higher than the rate the W Family paid under the initial swap terms. And even if the W Family was able to achieve a better rate than it would otherwise have been able to command because of the “multi-callable” nature of the arrangement (for example for a ‘cap’), this does not of itself make that arrangement ‘fair’ – especially if, as in this case, it is clear that the customer was not aware of the implications of the multi-callable arrangement and the risks it imposed on the customer. In any event, I remain of the view that the “multi-callable” structure was effectively a one-sided deal included largely for the commercial convenience of the bank.

The length of the swap itself also appears to me to be a significant issue. Small businesses are not well suited to make fixed long-term commitments. While it is true that the family had entered into a 14-year loan to purchase the 'new' hotel, the exit strategy from the decision was reasonably clear (i.e. by selling a hotel) and there were opportunities to either expand (as the family of course hoped) or contract the business from that base.

The swap in contrast assumed a 15-year life and in present circumstances imposes an almost insurmountable burden on the family, effectively eradicating any room for any exit strategy or financial manoeuvre that the family might otherwise have had.

My conclusion therefore is that the hedging met some of the family's needs in that it provided some short-term discounted protection from interest rate variation. But for the reasons set out above the particular swap was not suitable for the needs of the family as a modestly sized business. Accordingly, Bank E should not have recommended it to the W Family.

In any event – or alternatively if I am not correct in concluding that the bank gave advice – it is relevant to consider whether or not the family had sufficient information to make an informed choice about whether or not it should itself decide to purchase the swap.

So, the other question I need to answer is:

- if the bank did *not* give advice, whether it gave the W Family information that was clear, fair and not misleading – in order to put them in a position where they could make an informed choice about the swap arrangement?

My conclusion is that the bank did not provide information that was clear fair and not misleading – and it did not pay sufficient attention to the information needs of its client. The bank knew that the family had limited experience and access to professional advice. It knew that the product it was selling was, by any standards, complex. Critically, in my view, it failed to draw adequate attention to the potential impact of cancellation costs on the transaction.

The term in respect of the early termination of the swap was, at best, opaque. The simple reality was that charges for cancellation could (and have) amounted to around a quarter of the total loan sum. Even if such terms were not uncommon at this time, by any standards that is an onerous provision, at least in its real world impact – and unusual, at least from the perspective of the family.

Crucially, nowhere in the documentation made available to the family (either before or immediately after the transaction) is there a clear statement of the possible scale of the fees involved in cancellation. The fact that there might be charges (or benefits) is clear, but not the scale of the possible quantum.

While I accept that the current interest rate position was not generally expected – and might fairly be described as distinctly unusual (at least in UK terms) – the possibility of rates being materially lower than the swap level was a real possibility. That this could give rise to very material breakage costs was clear and the bank understood the risk associated with this investment product. Similarly, I note that the way in which the swap worked did not lend itself to simple explanations of precise sums. But illustrative examples of the range and nature of possible costs were practicable – yet were not provided.

My overall conclusion is that Bank E acted unfairly in its dealings with the W Family. It gave them advice to purchase a swap that it knew (or should have known) was a poor fit for the family's needs. And whether or not it gave advice, it encouraged a focus on short-term rates while it effectively hid the potential impact of cancellation charges. This had the effect of tying the family into a 15 year arrangement that has not met their needs.

Bank E introduced the idea of interest rate hedging to the W family at a point when they were already committed to the borrowing – and had little opportunity to consider the matter carefully or change their minds – despite the bank having formed the intent much earlier that the interest rate risk associated with the loan should be hedged.

The final paperwork signed after the arrangements were put in place has no requirement on the family to enter into the swap agreement to obtain the loan. But the internal Bank E paperwork leading up to the sale makes clear that, in the mind at least of the bank officials, there was a strong connection between acceptance of the swap and agreement to the loan.

So I find the family's account that it understood that the swap was a *requirement* of the loan to be credible. But the suggestion that the swap was required in this case for loan security or similar considerations is weakened by the failure to make it a formal requirement in the loan agreement. It is also significantly weakened by the fact that the bank put in place a "multi-callable swap" that, for the reasons I have explained, gave no real protection from significant rate increases (the very security consideration that is often argued as justifying the requirement to put in place a swap).

Instead, as I have already remarked, it seems to me that in this case the swap was put in place primarily for the bank's commercial convenience and with little or no attention to the needs of its client.

uncertainty and hindsight

Before reaching my conclusions on fair compensation in this case, it is appropriate to sound a note of caution about the risks of hindsight in the present case.

Consumers who freely entered into an arrangement to "fix" interest rates at what now appear high levels will understandably now regret the decision they made. But the fact that we all now know that base rates are at (UK) record lows – and have remained so for over three years – does not of course mean that this was predicted or expected. Indeed, given the history of (UK) interest rates, some customers in 2007 may well have felt that increases in rates well above 6% were a very real risk.

And while major banks such as Bank E might reasonably be assessed as having better knowledge of the risks inherent in the long-term fixing of interest rates and the potential for interest rate volatility, it clearly cannot be expected to have had a crystal ball. The present position on interest rates was not widely predicted in 2007, even in financial circles.

But the inherent variability of interest rates was understood. In the UK, in the 20 years prior to 2007, base rates had varied from 14.875% in October 1989 to 3.5% in July 2003. Internationally, even amongst the present G20 economies, the range of variation had been much wider. The US base rate fell to 1.13% in 2003, while Japan's base rate has not risen above 1% since 1995.

International comparisons are fraught with difficulties. But the possibility of retaining low or even 0% rates was clearly not out of the question. So while the present position may not have been a central prediction in 2007, it was not in my view such an exceptional position (in relation to interest rates) that it could be accurately discounted as “it can never happen in your lifetime”.

And of course rates did not need to be as low as they are today for there to be a very substantial cancellation charge under this swap.

fair compensation

I have found that Bank E gave inadequate information to the W Family to enable them to make an informed choice and that it gave unsuitable advice.

Clearly, I cannot now be sure what the W Family would have done had the full potential impact of the various provisions of the swap agreement been brought to their attention. Recollections now of perspectives in 2007 will inevitably be uncertain or affected by subsequent events.

The paperwork at the time gives the impression that the W Family were excited by their new venture and keen to make the transaction – but also reasonably cautious and risk averse. The bank itself had described them as cautious. The family was, perhaps inevitably, interested in minimising short-term expense (hence the attraction of the swap deal that offered an initial discounted period).

And the family clearly saw benefit in guarding against any possible increase in rates, at least in the short-term. It had ambitions for the future. But it was also a relatively modest sized family business. Its fortunes rested not just on its hotel market but on the welfare of the family owner-managers. The business clearly had potential but there were also risks and uncertainties.

Overall, while no doubt the family envisaged a successful long-term future they would, it seems to me, have been reluctant to make unnecessary long-term commitments that might tie them into particular financial arrangements. Certainly the family might have been well advised to avoid such long term commitments.

Subsequently Bank E sought to rely on those terms that it knew it had not explained or highlighted adequately to make charges of around £500,000. The decision by Bank E to rely on them in 2009 had the effect of significantly narrowing the W Family’s room for manoeuvre when flexibility was particularly important to them.

Bank E has commented that the W Family entered into a long term loan and that it had not been disputed the family was aware of the 15 year term of the swap agreement. This, the bank argues, demonstrates that the W Family was willing to make long term commitments. But I noted above, the exit strategy from the loan was clear – to sell the hotel and repay the borrowing –while the swap offered no such straightforward exit. I do not disagree that the W Family was aware of the lengths of both the swap and loan they had agreed to. However, I do not consider the effect of these terms can be considered equivalent given the potential break cost associated with the swap and the degree it could reduce the flexibility they will have required.

Of course, at one level, the W Family's circumstances are no better or worse than predicted. The interest rate on their loan was effectively collared at the swap rate and continues to be so. But the cancellation charge on the swap makes any release from that arrangement effectively impossible. The W Family might well have expected cancellation charges, but not ones accounting for around a quarter or more of the overall loan value.

In cases such as these, mapping the path of what might have occurred – and the implications of any differences – can be complex. What alternative arrangements would the W Family have made in 2007? If they had not faced such a (large) break cost in 2009, what would they have done to rework their finances?

What impact would all these differences have made to their current position? Considerable time and expense for all parties could be spent in debating each of these issues (and the numerous subsidiary issues that these would entail).

It appears to me that it would have been in the interests of both parties to identify ways of unravelling the current position that are fair and, crucially, give the family the best opportunity to maintain and safeguard their business, if that was possible. However, as it has not been possible for the parties to agree a way forward it is necessary for me to reach formal findings on redress.

The aim of any award I make is, as far as is reasonably practicable, to place the W family in the position they would most likely have been in had the bank offered suitable advice and/or met the family's information needs. While the exact position cannot now be identified I am satisfied it is possible to reach a conclusion on fair compensation.

In response to my provisional decision, Bank E appears to have suggested that since the W Family were incorrectly led to believe that hedging was a condition of their loan, they would have hedged for much longer than the two years I suggested in my provisional decision. I find this argument, at best, unconvincing.

I conclude that the W Family believed hedging was required because they were provided with insufficient information, and that the information provided was not 'clear, fair and not misleading'. It is therefore unreasonable for the bank to rely on this position when suggesting what the W Family would have done if not for the unsuitable advice and/or inadequate information provided.

On the basis of the information available to me from the relevant time – and in considering how fair compensation should be assessed – I conclude on balance that the family would not have chosen this swap but for the errors made by the bank. For the purposes of assessing fair compensation I conclude that had the family been properly advised (and/or properly informed about the product) it would on balance have *instead* entered into an agreement to fix interest rates for a shorter period and not one which included such significant termination provisions. In reaching this conclusion I recognise that such a product may not have been made available at the time by Bank E.

In the present case I also note the initial discounted rate was provided by Bank E on the basis of a higher rate for the remaining 13 year term. So the pay rate for a shorter-term fixed rate would have been higher than the rate the family paid under the initial swap terms.

I appreciate the W Family has provided a redress proposal in order to come to a mutually agreeable settlement to this dispute. And I am aware that some have argued that in cases such as this, given the failings by the bank, the logical conclusion of any redress should simply be to remove the 'unfair' swap and compensate the customer accordingly. However, it is well established both in the courts, and in the decisions of this service, that the appropriate approach to redress is to consider what would have happened had the 'unfair' transaction not taken place and to contrast the position of the customer following the poor advice with that which would (probably) have occurred but for that poor advice.

Clearly in some cases this may mean that no purchase would have been made at all. In other cases, despite the poor information and/or advice, the consumer may have made the purchase in any event (sometimes this is referred to as the insistent consumer). But in many cases the customer is likely to have made alternative arrangements. Having considered the position carefully I think this is such a case. That is the W Family would have made alternative arrangements. I say this because it was clear that the family was concerned to keep its initial costs under control as it established the new business. It could not afford for rates to rise significantly. The discussions with the Bank at the time notes the W Family's concerns about its position over the next two years. But unlike the Bank, I do not see that the W Family would have made a long term commitment in this case to hedge rates.

Clearly this is a matter of judgement, but in my opinion, fair compensation should be based on a shorter hedging arrangement rather than on removing all arrangements entirely. It follows that fair compensation in this complaint does not need to take into account any compensation to Bank E (i.e. break costs). The shorter agreement would have expired and there would be no compensation due to Bank E in order for the W Family to have reverted to the variable rate applicable to the loan agreement after two years.

I recognise that the Family feels that the existence of the swap has hung over their heads for the past three or more years. They have drawn my attention to losses and costs they say they have incurred that they may well *not* have incurred had the bank acted reasonably. In certain circumstances losses directly flowing from the errors of the bank might justify an award of compensation in cases such as this. However, in this case – while I understand the family's concerns – I am not satisfied that on balance these matters flow directly from the problems caused by the swap rather than, for example, wider trading conditions.

The W Family explain they feel the circumstances in their case are exceptional and warrant a payment to cover professional costs. I note these costs have largely been borne out of the W Family's ongoing relationship with the bank since 2011, and not in pursuing their complaint through the Financial Ombudsman Service. That is, the professional costs are being claimed as consequential losses caused by the breakdown in the customer-bank relationship and the family's desire to understand their position.

I am not persuaded to make an award with regard to any professional costs incurred by the W family in bringing the complaint to us. The Financial Ombudsman Service is an informal service and professional representation is not normally required. I am satisfied that in this instance, the complaint could reasonably have been brought to us without professional assistance.

In contrast to the Family's observations, Bank E has forwarded proposals for redress with statistics based on a methodology its independent 'Skilled Person' (as required by the FCA review) has agreed to. These proposals significantly differ from what I consider to be fair compensation in my provisional decision.

Bank E says the following are its key points in relation to the redress:

- *The sale of a £2m bullet Bermudan callable swap against £1m LIBOR was not suitable for this customer and various aspects of the Bank's sales process were inadequate, including the standard of disclosure around break costs and the nature of the bullet Bermudan profile and resultant hedging mis-match.*

- *There was a however a legitimate condition of sanction to hedge a minimum of 50% of the loan and the evidence shows that the basis and requirements for this hedging, including options to achieve [the W Family's] desired payment profile were actively discussed prior to the trade. It was fair and reasonable for a hedging product to be in place.*

- *Fair and reasonable redress has been assessed to be the implementation of an alternative product that deals with the unsatisfactory features of the product actually sold, together with a refund of the difference in cash flows between the actual and alternative products, plus interest at 8%, as follows:*

    - *The callable features of the original trade are inappropriate and will be removed. The swap will be amended to a simple vanilla swap without call options;*

    - *The notional profile will be amended to accurately reflect the known repayment plans of [the W Family]. The replacement notional profile will be based on £2m for the first 3 months, £1m for the next 6 months and amortising for the remaining 14 years;*

    - *The initial rate of 4.38% for two years, per the original trade will be maintained as it is in line with the [the W Family's] original desire for a low starting rate. A new stepped up rate of 6.73% will be applied for the remaining 13 years – this reflects market pricing for the alternative product at the time of the original trade;*

    - *The index mis-match that exists due to the original swap being against £1m LIBOR whilst the loan rate being linked to base rate will also be redressed, although no detriment has occurred to date as a result of this mis-match.*

- *Bank E says the result of the above redress actions would be a refund of historic cashflows plus interest which the Bank has provisionally calculated as £252,295. In addition, the 'mark to market' of the alternative product is £548,451 less than the actual product sold. The Bank notes that in its proposed approach it would cover this cost.*

- *Bank E also note that in addition to the calculation of redress in relation to the alternative product set out above, the Bank would need to engage with [the W Family] in relation to any claims for consequential loss on the basis set out by the FSA for such claims as part of the review of these sales.*

Bank E says that the redress set out above has been determined to the requirements of the FSA Review methodology and agreed by the independent Skilled Person. It argues that whilst some aspects of the redress determination here differ from my provisional *award, they result in a settlement significantly in excess of the £100,000 maximum award I can make..*

I have considered Bank E's proposal carefully. However, I do not agree that the redress calculated by Bank E is fair and reasonable in the circumstances. Bank E says its proposal is made in line with the regulator's required approach for its review of such sales. I disagree. I would be surprised if this conformed to the regulatory requirement for redress in these cases. But in any event it does not appear to me to be fair compensation, as for the reasons set out above, I do not agree with Bank E's proposal in relation to the alternative product. I also consider that Bank E's proposal on how to calculate compensation due in relation to the difference between a revised product and the swap the W Family actually took is likely to under-compensate the W Family for the losses that they incurred.

In my view the calculations on redress should be a full re-working of the account, to place the W Family in the position it would have been in had it been sold the alternative product. This means a full reconstruction of the W Family's account based on how payments (and any associated costs or credits) would have been.

Bank E also says that the methodology it has agreed with the FCA and Skilled Person requires that it presents all redress offers directly to the customer in the presence of the Skilled Person to ensure that the findings of the review are correctly represented to the customer. Bank E has asked me to confirm I am content for it to contact the W Family to arrange the redress presentation due as part of the review. This is a matter for the Bank and the FCA, not for me. But in any event I am not convinced that there is any need for my decision to be further delayed by any such meeting or the further considerations by Bank E about its obligations under the regulatory review.

The bank's review of its sale to the W Family (as required by FCA) will no doubt proceed as is appropriate for Bank E's regulatory obligations. If it transpires that the W Family later thinks any compensation proposed by Bank E under its review would be more beneficial than the redress I propose, then it would be open to W Family to accept the outcome of the review.

my final decision

For the reasons set out above, my final decision is that I uphold the W Family's complaint. This "multi-callable interest rate swap" should not have been recommended to the W Family by Bank E – and Bank E should have provided better information in relation to the product it sold.

Where I uphold a complaint, I have the discretion to make a money award requiring a financial business to pay fair compensation, plus any interest and/or costs that I consider appropriate, and/or I may make directions requiring a financial business to take certain actions. In the circumstances of this case, I have done both.

determination and award

I uphold the complaint.

I order Bank E to rework the W Family's accounts as though a two year interest rate swap agreement at the higher rate of 5.95% (rather than the initial discount rate of 4.38%) was put in place from the outset.

This action will reflect the following practical considerations:

- At the end of the two year swap no new product would have been put in place, and future payments against the loan would have been settled on the basis of underlying variable rate borrowing on an on-going basis.

- If re-working the arrangements results in the W Family having made overpayments, as it seems likely, Bank E should refund those overpayments.

- Overdraft interest, charges and fees, and any loan fees, paid by the W Family which it would not have paid on the re-worked accounts should be refunded with effect from the date they were paid.

- Bank E should also review in full the accounts of the W Family and reconsider any discretionary actions such as margin renegotiations or placing the accounts into 'the business support group' or other special measures. I do not propose to interfere in the bank's legitimate commercial decisions in this regard but it is fair that the conduct of the re-worked account be the relevant factor in the application of that discretion.

- If Bank E believes it is legally obliged to deduct tax from the interest, it should send a tax deduction certificate with the payment. The W Family may then be able to reclaim any tax overpaid from HM Revenue and Customs, depending on the circumstances.

I am mindful that if a final decision is accepted by the W Family the maximum binding money award I can make in this case is £100,000. (I note that had the family referred the matter to me after 31 December 2011 that limit would be £150,000). Having regard to the sums paid to date in this matter, I am mindful that the money award I recommend may exceed this limit. Given the circumstances of this complaint, I recommend that the bank should pay any and all sums I have concluded would be fair compensation and which are above the maximum money award. Although I note Bank E is not under an obligation to meet this recommendation, I note it has previously indicated it will pay the amount in full. In any event I require Bank E to notify the W Family whether it will accept my recommendation by 2 August 2013, and to copy me in to this correspondence.

The W Family should note that if Bank E refuses to accept my recommendation, the law is unclear as to whether they would be able to accept my decision and go to court to ask for the difference.

Under the rules of the Financial Ombudsman Service, I am required to ask the W Family to accept or reject my decision by 27 September 2013.

Tony Boorman
deputy chief executive & deputy chief ombudsman