

The complaint

M, a limited company, complains about delays in arranging a commercial mortgage, which it says meant that AIB Group (UK) Plc ended up lending at a higher interest rate than it should have done.

What happened

M is a limited company which has a commercial mortgage with AIB. M meets the micro-enterprise test and is therefore an eligible complainant under our rules.

M took out its first loan in 2017 – the loan was agreed in December 2016, with funds drawn down a few months later. The loan was for five and a half years to fund the development of M's business. After the first six months, the loan moved on to a fixed interest rate for the remaining five years. The fixed rate was described in the loan agreement as "3.75% above the fixed cost of funds rate" – the fixed cost of funds rate being set on the date the funds were drawn down.

The loan was due to come to an end in November 2022 and would need to be repaid or re-financed at that point. On 15 August 2022, concerned about rising interest rates, one of M's directors – who I'll call Mrs P – contacted AIB to ask about ending the existing fixed rate and re-financing early.

M says it didn't get a proper response to this request. In early September it was contacted by AIB to discuss the upcoming end of the loan. Mrs P says she was concerned to be told that re-financing would require a full new application rather than a brief review, as she said she'd been led to believe at the time of the first application in late 2016. She also complains that she still hadn't been given the break cost figure to enable M to decide whether it would be better to take a new fixed rate immediately or wait until November.

AIB told Mrs P that M could break the fixed rate immediately and go on to a variable rate. Or it could apply for a new fixed rate to take effect on a new loan agreement from November. A new fixed rate was likely to be around 7.75% - 3.75% above the 4% cost of funds.

On 21 September AIB offered to reduce the 3.75% margin to 3.35% - this was because it accepted it had delayed by around two weeks in responding to M's initial request in August, and it said this would reduce the fixed rate M could now obtain to what it would have been able to obtain in August. But the actual interest rate to be paid could not be determined until an application had been completed, as that would determine the cost of funds available on that day. The fixed rate was booked on 27 September, which meant the interest rate on the loan was 8.611% - cost of funds of 5.261% plus the reduced margin of 3.35%.

AIB didn't think it had acted unfairly. It had offered to reduce the margin to reflect that there was some delay in responding to M's initial contact – this covered the increase in the cost of funds M would have had to pay because of the delay. But it said that a full new application was required to re-finance the loan after November 2022, and the actual interest rate could only be determined on the day the fixed rate was booked. That was 27 September 2022 – and the reduction in the margin covered the increase in cost of funds compared to what

could have been obtained had it been booked sooner.

M complained to us. It said a ten year facility had been agreed in 2016 – so all that should have been changed in 2022 was the five year fixed rate. It said that had AIB responded to its request in August, it would have been able to secure a rate of around 7.25%

Our investigator thought that AIB had delayed in implementing the new fixed rate, at a time of rising interest rates. He said it had taken AIB around two weeks to get to the point of booking a new rate from the time it started the process in mid-September. If AIB had started arranging the new loan when Mrs P first contacted it in mid-August, M would have been able to book a new rate around 29 August. So AIB should amend the loan as if M had booked a rate on 29 August not 27 September, using the cost of funds rate available on that date. He said that AIB should confirm whether the 0.4% discount it had already offered was sufficient to achieve that. And he said AIB should pay M £150 compensation for the inconvenience caused.

AIB didn't accept that. It said it didn't agree that M would have been able to book a rate before 27 September. It said that M hadn't decided to go ahead with a new loan application on 15 August, it was just looking for information about its options. It accepted that it had delayed in responding to Mrs P's questions. But it said that once it had understood that it had treated the application as a priority and fast-tracked it, so that it completed in much less time than would usually have been the case. Had nothing gone wrong, M would still have secured a rate around the end of September, so it wouldn't be fair to require AIB to offer a rate that was available in August.

Having looked at all the evidence I took a different view. So I issued a provisional decision setting out my thoughts to allow the parties a further chance for comment.

My provisional decision

I said:

"I've thought carefully about everything that's happened here. Both parties have provided detailed evidence about the timescale of events from their point of view.

While there's disagreement about the details, the bigger picture is not in dispute. Mrs P, on behalf of M, first contacted AIB to ask about the cost of breaking the existing fixed rate on 15 August but AIB didn't carry out the calculations or give Mrs P the information she'd asked for.

Separate to Mrs P's request, AIB got in touch with M on 7 September to discuss the upcoming end of the loan and the possibility of re-financing. This was a scheduled contact ahead of the end of the loan term and wasn't in response to Mrs P's contact in August.

Incidentally, I don't think Mrs P is right that this was or was intended to be a ten year loan. The loan agreement from December 2016 is clear that the loan is over a five year term. Mrs P has referred to a letter offering a loan which says "loan repayments have been calculated over a 10 year term with a 5 year review on same as per your facility letter" but this letter is dated 3 December 2015, not 2016. It's not clear whether that's a drafting error and it should be dated 2016, or whether it's a record of an earlier discussion pre-dating this loan. As the interest rate in the letter is also different to the interest rate in the loan agreement, that suggests it's related to earlier discussions about a different loan. But in any case, even if the letter is about this loan and the date is an error, the agreement is set out in the facility letter (loan

agreement) not the letter. And the loan agreement is clear that the loan is over a five and a half year term.

That means that the application in 2022 wasn't a simple interest rate switch. It was a new application for a new loan to replace the existing one. That included a new valuation and new underwriting checks.

In August, M hadn't decided what to do. The initial contact was about the cost of breaking the existing fixed rate, which ran until November. At this point, the options open to M included continuing with the existing fixed rate but applying for a new loan to follow on, continuing with the existing fixed rate while looking to re-finance with another lender, or breaking the existing fixed rate and moving on to a variable rate for the remainder of the term until November – after which the same options about the future would apply. If M decided to apply for a new loan with AIB from November, it could take a fixed rate or a variable rate.

What should have happened was that AIB explained this to M in August. That didn't happen. It was only following the contact on 7 September that things started to move. M decided not to break the existing fixed rate and move on to a variable rate for the rest of the term because the variable rate wasn't lower than the existing fixed rate.

The application for the new loan from November then began to move ahead. Mrs P says that a valuation was a waste of time because the property had increased in value, and the loan amount reduced, since 2016. That may well be true. But that doesn't mean it was unnecessary or unreasonable for AIB to carry out a valuation. It's standard for new lending – which this was – and enables AIB to confirm that there are no issues with the property which have arisen in the meantime and that it meets AIB's current lending criteria. I'd always expect a bank to require a valuation in situations like this.

The application then proceeded, and an offer was issued on 21 September. M signed and returned it and booked a new interest rate on 27 September.

The interest rate for this loan, like the earlier 2016 loan, is a fixed rate and based on two elements. There's the cost of funds rate, and a margin. The cost of funds rate changes all the time, and reflects the cost to AIB of raising the money it lends to M. These costs are not directly linked to Bank of England base rate, but reflect changes in the money markets. The margin is the fixed amount above the cost of funds rate that AIB charges – this represents the amount it needs to charge above the cost of raising the funds to cover matters such as its operating costs, risk, and reasonable profit.

The margin is set out in the loan facility letter. The cost of funds rate is set on the date the interest rate is booked and the funds to lend allocated.

M booked the new interest rate on 27 September, when the cost of funds rate was 5.261%. M's complaint is essentially that this rate was increasing throughout August and September, and so if AIB hadn't delayed in responding to the initial enquiry in August, M could have booked a rate in late August or early September, substantially reducing the rate it would have to pay over the term of the new loan from November.

I've thought carefully about this. But I'm not persuaded, on balance, that M would have been in a position to have booked a rate much sooner than it did.

In the first place, M hadn't decided to take out a new loan from November at the time

of the first contact in August. Mrs P says that even in early September it was looking at other alternatives to see if it could get a better rate elsewhere.

Secondly, even if M had decided to apply for a new loan in August, I don't think the process would have happened much more quickly. When Mrs P complained in early September about the failure to provide the break cost as requested, AIB recognised it had made a mistake and it expedited the new loan application. It ensured it was passed to the relevant people internally more quickly, and also took other steps to speed things up – such as arranging a valuation alongside the underwriting rather than afterwards as would usually be the case. The result was that a loan application that would usually take around six weeks took from 9 September to the issue of an offer on 21 September.

In other words, if AIB had started the process in mid-August and processed it within its usual timescales, the offer would have been issued in late September, allowing M to book a rate at the end of September. By expediting the process because of the delay at the start, AIB ensured that M was in the same position, with the offer and rate booking happening around the same time as they would have done without the initial delay. In addition, AIB also reduced its margin from 3.75% to 3.35% - reducing the overall interest rate by 0.4%. I think this fairly compensates M for the delay in getting the process started. I don't think it would be fair to require AIB to give M a cost of funds rate that was available in late August, as that would never have been possible even if nothing had gone wrong from the start.

The external context in which this application happened is that, because of events in the wider economy, this was a time of rising interest rates. AIB isn't to blame for that. But it explains why Mrs P was so worried about identifying M's options and securing a rate as quickly as possible – and why she's complained that the rate has increased because of AIB's delay. As I've explained, I don't think that is the case – but I can see why Mrs P would be worried that it was.

The reality is that I think M was simply unfortunate. It could see that interest rates were rising – and so any delay in securing a new rate risked the rate it ended up with getting ever higher. So once the facility letter was in place, it booked a rate as soon as possible at the end of September. This was understandable given what had happened up to that point.

M didn't have to do that. It could have opted for a variable rate – or it could have booked a fixed rate later, in October or November. The cost of funds rate peaked in late September / early October, so if M had waited we now know, with the benefit of hindsight, that it could have secured a lower rate. But it actually booked a rate at the top of the market.

That couldn't have been known at the time. But the context of rising rates explains the sense of urgency Mrs P felt, and her frustrations at the delay M experienced. Ultimately, though, I think AIB put things right in a fair way. It expedited the application so that the offer letter was issued around the time it would have been without the delay, and it also reduced its margin. The decision to book a rate, and when to do so, once the offer letter had been issued was M's.

Finally, M also complained about the start of the new loan. AIB didn't collect the final payment on the old loan, instead adding it to the balance of the new loan. It shouldn't have done that without consulting with M – because doing that rather than allowing M to make the payment increased the starting balance of the new loan.

AIB has put that right by reducing the loan balance by the amount of the interest that will be charged on this additional balance over the loan term. This means that M won't be charged any extra interest because of the extra borrowing represented by the uncollected payment.

M says that the loan repayments are still higher because of this – while that's true, because of the reduction in interest they are only higher by the amount of the November 2022 payment spread over the term of the new loan. While M will have to pay that amount over the term, it didn't have to pay it in November 2022. The amount of the November 2022 payment M has saved is the same as the total of the extra amounts it will have to pay over the loan term, and so M has not suffered any financial loss following the reduction of interest."

The responses to my provisional decision

M didn't agree with my provisional decision. It said that AIB had told it that it would take around two weeks to set up a new rate. It referred to an email from an AIB staff member, dealing with its initial complaint about failing to make contact in August 2022, which said "I believe two weeks would have been a reasonable timeframe from initial enquiry [to re contract] ... It is reasonable to assume we may have been in a position to re-contract on 30 August." M said that it therefore didn't agree with my assessment that six weeks would have been a reasonable timescale – and that the difference had an impact on the outcome reached.

AIB said it had nothing to add.

What I've decided – and why

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

I've also considered what I said in my provisional decision, and I've considered M's response to see whether it changes my mind. I'm afraid it doesn't. I accept AIB sent Mrs P the email referred to – I saw it and took it into account in reaching my provisional decision. But I'm not persuaded that what the email says is correct in light of all the other evidence about what was actually required.

In the first place, I don't think that – even if a two week timescale was realistic – it would be fair to take the timescale as starting from M's initial contact to AIB in mid-August. At that point M had not decided to re-contract with AIB. Its enquiry was about the possibility of breaking the existing fixed rate, not starting a new loan agreement from November. That may have been because M mistakenly thought that the loan agreement continued beyond November and all that would be required then is a new interest rate not a new loan. But it's also clear from what M has said that in August it wanted to know about the cost of breaking the existing fixed rate so it could consider its options. M wanted to know what the break cost would be so it could look at the market and decide whether to ask AIB for a new fixed rate, or whether to move the loan to another lender.

If, then, AIB had answered the initial enquiry promptly in mid-August, it would have told M what the break cost was and then M would have gone away and thought about its options, including consulting with other lenders. It wouldn't have started the re-contract process with AIB there and then. It follows that even if AIB hadn't delayed at this stage the re-contracting process would not have started in mid-August and – even under a two week timescale – would not have finished by 30 August.

I also don't think the two week estimate given in the email is actually realistic under normal circumstances. In September AIB actually achieved that timescale, but only by expediting the process internally and by carrying out the valuation alongside the underwriting process rather than afterwards; steps it took to resolve M's complaint. A normal application would have taken more than two weeks.

Had AIB responded to M in mid-August and provided the break cost as required, I think it's likely M would have taken some time to consider its options and explore the market, as it said it would do. If, having done so, it had decided to remain with AIB I don't think it's likely it would have made that decision until late August or even early September. If that had happened, issuing an offer on 21 September – which is what actually happened – would still have been quick. For those reasons, I don't think AIB's failure to respond to M's initial contact resulted in an offer that was issued any later than it would otherwise have been.

Finally, the setting of the fixed rate is separate to the loan re-contracting process. Once AIB agrees to lend and issues a loan offer, the borrower then has the option of selecting a fixed or variable rate at any time up to drawdown. The fixed rates available on any given day change from time to time. I've said that I don't think the offer would have been issued any sooner even if AIB had responded to M in mid-August. Once the offer was issued, it was then up to M to decide when to select the rate it wanted. It was M's choice to book a rate on 27 September, when rates were close to their peak. If M had waited, it might have been able to secure a lower rate as they fell from mid-October. But even if nothing had gone wrong it would never have been able to select a rate before the peak, in early September, as an offer would never have been issued by then.

I do think AIB should have responded to M promptly, with the break costs, when contacted in mid-August. But I don't think the failure to do so caused M any financial loss, since the new loan would always have been offered around the same time as it actually was. And while the delay undoubtedly caused M inconvenience, and its directors found that upsetting and frustrating, AIB has reduced the interest rate on the new loan agreement by 0.4% for the duration of its term. This will reduce the interest M would otherwise have had to pay over the new term, and I think that's fair compensation in all the circumstances.

My final decision

My final decision is that I don't uphold this complaint because AIB Group (UK) Plc has already made a fair and reasonable offer to resolve it.

Under the rules of the Financial Ombudsman Service, I'm required to ask M to accept or reject my decision before 10 January 2024.

Simon Pugh
Ombudsman