THE HIGH COURT

[2013 No. 422 MCA]

IN THE MATTER OF AN APPEAL PURSUANT TO PART VII (B) OF THE CENTRAL BANK ACT 1942, AND CHAPTER VI AND SECTION 57CL THEREOF (AS AMENDED AND INSERTED BY THE CENTRAL BANK AND FINANCIAL SERVICE AUTHORITY OF IRELAND ACT 2004)

BETWEEN

KENNETH MILLAR AND DONNA MILLAR

APPELLANTS

AND

FINANCIAL SERVICES OMBUDSMAN

RESPONDENT

AND

DANSKE BANK

NOTICE PARTY

JUDGMENT of Mr. Justice Gerard Hogan delivered on 30th September, 2014

1. This is an appeal brought by the appellants, Mr. Kenneth Millar and Ms. Donna Millar, pursuant to the provisions of s. 57CL of the Central Bank Act 1942 (as inserted by s. 16 of the Central Bank and Financial Services Authority of Ireland Act 2004)("the 1942 Act"). In this appeal Mr. and Ms. Millar challenge a decision made by the Financial Services Ombudsman ("the Ombudsman") on 10th December, 2013 to reject their

complaint against the notice party, Danske Bank (formerly known as National Irish Bank)("Danske"). The appellants have seven mortgage accounts with Danske and the complaint relates to the manner in which Danske purported to increase the variable interest rate which is payable on those mortgages. The issue in essence relates to the definition of variable interest rate contained in the applicable terms and conditions governing the loan arrangements these parties.

2. In 2005 the Millars entered into seven separate mortgage loan agreements with Danske in respect of a number of residential properties. One of these properties concerned the Millars' own family home and the others were in respect of buy-to-let investment properties. It is agreed that the interest rate applying to loan was a standard variable rate. It is further accepted that these loans are currently being serviced and are not in arrears.

3. It is also important to state at the outset that it has never been contended that these mortgages were "tracker" mortgages, *i.e.*, where the interest rate tracked the interest rate set by the Governing Council of the European Central Bank ("the ECB"). The appellants' case is rather that, having regard to the terms of the mortgage deeds (and other extrinsic evidence), Danske acted wrongly in increasing interest rates at a time when interest rates generally have fallen to historically low levels.

4. Interest rates have fallen since the onset of the global financial crisis in 2008, save for a short period in 2011 when interest rates were (briefly) raised twice by the ECB. This decline in interest rates has been especially marked within the Eurozone since the latter months of 2011 as the future of the currency seemed in doubt and a series of rate cuts was then commenced by the ECB. While that threat seems to have passed – for now, at any

rate – the ECB has subsequently been faced with the new problem of acute disinflationary pressures within the Eurozone area. The difficulties which the ECB has encountered in recent years in meeting its own inflation target of 2% has resulted in a situation where interest rates have now been set at unprecedentedly low rates. Given this deflationary environment it seems likely that monetary policy within the Eurozone will continue to remain accommodative and, so far as can be presently judged, that interest rates will remain at these very low levels for the immediate future. Such is the broad economic backdrop to the present appeal.

5. The gist of the Millars' complaint is, however, that Danske have allowed its variable interest rate to increase at a time when interest rates within the Eurozone have fallen so dramatically. In their affidavit grounding these proceedings the Millars have demonstrated that in the period prior to October 2011 there was a very high - and, indeed, almost perfect – coefficient of-correlation between the interest rates applicable to their loans and ECB rates. In November 2011, however, Danske increased its variable rate by almost 1% and since then that rate has remained at just over 4%. In the meantime, following a succession of interest rate cuts, the ECB rate has plunged to almost zero. It is sufficient for present purposes to say that the rate gap between the ECB rate and the variable rate has widened from 1.5% to a figure of just over 4%. The Millars point out that there is now a "significantly imperfect negative" correlation between the ECB rate and the interest rate applicable to their loans. This analysis has not been contradicted by either the Ombudsman or by Danske.

6. The appellants complained about this increase in the variable rate, but Danske defended its decision to raise its variable interest rate on the basis that, as it did not

receive any ECB funding, these rate cuts were irrelevant to it. Following further correspondence between the parties, the matter ultimately proceeded to the complaint stage. The complaint was ultimately rejected by the Ombudsman by decision dated 10th December 2013.The relevant portion of the Ombudsman's decision is in the following terms:

> "The complainants entered into a number of mortgage agreements with the Bank. The Bank has provided a copy of each of the loan agreements in evidence including the applicable terms and conditions for each agreement. Clause 3 of the general terms and conditions is the same for each agreement and states:
>
> > 'Rates of interest are altered in response to market conditions and may change at any time without prior notice and with immediate effect.'
>
> The complainants assert that the Bank is only entitled to amend or alter the applicable rate of interest 'in line with the general market interest rates'. The complainants therefore argue that the Bank's decision to increase the rate of interest when the ECB rate has declined is a breach of the agreement. The term 'in line with general market interest rates' referred to by the complainants is not included in any clause of the terms and conditions. Clause 3 of each of the loan agreements is clear in its wording and permits the Bank to increase the interest rate 'in response to market conditions'. Under the terms and conditions of each of the loan agreements the Bank is not restricted by reference to the ECB rate when it is assessing the appropriate rate of variable interest. The Bank's obligation under each of the agreements is to alter the rate in response to 'market conditions' and not 'in line with general market interest rates'. The Bank is acting in

accordance with the terms and conditions of each of the loan agreements in altering the variable rate of interest in accordance with market conditions and there are no grounds for establishing that the Bank is obliged to disclose the basis on which this assessment is calculated. Therefore this aspect of the complaint is not upheld."

7. The Millars also referred to an explanatory note for customers which was contained on the Bank's website and which, they contended, provided an explanation of the Bank's variable interest rate. The printout from the website, which is exhibited in evidence, was dated 4th March, 2009, and the Millars contended that this statement (or something very like it) was in existence when they entered into these mortgage agreements in or about 2005. In that website printout the term "variable rate mortgage" is described as:-

"As the name suggests, the interest rate you pay on a National Irish Bank variable rate home loan changes in line with any fluctuations in general interest rates. When interest rates go down your monthly payments do likewise. However, when interest rates rise, your monthly payments will increase too. You can also make lump sum repayments at any time without any penalty."

8. Indeed, in their complaint to the Ombudsman dated 22nd May 2013, the Millars drew attention to the fact that the information posted on Danske's website stated that the "interest rate you pay on a National Irish Bank variable home loan *changes* in line with any fluctuations in general interest rates." (emphasis supplied) The Millars further stated that at sometime after February 2009 this website posting was changed so that customers are now informed that the "interest you pay on a National Irish Bank variable rate home

loan *may change* in line with any fluctuations in general interest rates." (emphasis supplied).

9. The Millars further contended in that complaint that they had received assurances from the Bank's staff at the time of entering into the loan agreements that "the variable rate loans would be subject to the market forces ensured by the fact that the same reference rate would apply equally to all of the Bank's mortgage customers and in line with general market interest rates."

Whether this Court should defer to the Ombudsman on questions of contractual construction

10. The fundamental question with which this Court is confronted on appeal is whether the Ombudsman's construction of clause 3 of the applicable terms and conditions discloses an appreciable legal error. The resolution of this issue raises once again the fundamental question: what is the true role and functions of the Ombudsman? Specifically, where the Ombudsman deals with a contractual dispute by applying principles of contract law, what attitude, then, should the court take where a disappointed party seeks to appeal to this Court? Should it defer to the Ombudsman on question of contract law or should the Ombudsman's decision be scrutinised as if it were, in effect, a decision of a lower court dealing with a contract issue?

11. The Ombudsman is required by s. 57BB of the 1942 Act to deal with consumer complaints in an informal and expeditious manner. Section 57BK(4) of the 1942 Act further provides that the Ombudsman is also required:-.

> "to perform the functions imposed, and exercise the powers conferred, by this Act free from interference by any other person and, when dealing with a particular

complaint, is required to act in an informal manner and according to equity, good conscience and the substantial merits of the complaint without regard to technicality or legal form."

12. Section 57CI(2) which provide that:-

"(2) A complaint may be found to be substantiated or partly substantiated only on one or more of the following grounds:

(a) the conduct complained of was contrary to law;

(b) the conduct complained of was unreasonable, unjust, oppressive or improperly discriminatory in its application to the complainant;

(c) although the conduct complained of was in accordance with a law or an established practice or regulatory standard, the law, practice or standard is, or may be, unreasonable, unjust, oppressive or improperly discriminatory in its application to the complainant;

(d) the conduct complained of was based wholly or partly on an improper motive, an irrelevant ground or an irrelevant consideration;

(e) the conduct complained of was based wholly or partly on a mistake of law or fact;

(f) an explanation for the conduct complained of was not given when it should have been given;

(g) the conduct complained of was otherwise improper."

13. A further critical consideration, however, is that the resolution of a particular complaint by the Ombudsman will generally create a *res judicata*. Thus, in *O'Hara v. ACC Bank plc* [2011] IEHC 367 Charleton J. observed:-

> "To all intents and purposes, it is clear that the allegations made in the complaint before the Financial Services Ombudsman are the same as those which are sought to be litigated in these proceedings. The nature of the jurisdiction conferred on the Financial Services Ombudsman by the Oireachtas cannot be ignored. It would be contrary to the statutory scheme and it would also be unfair for parties to a complaint before the Financial Services Ombudsman to be later subjected to very similar litigation. The legislation has made any determination by the Financial Services Ombudsman subject only to an appeal. Absent a special reason of sufficient impact to nullify any potential abuse of process, it would be wrong for this Court to say that complaint could be re-litigated all over again. Such a finding would undermine the will of the Oireachtas."

14. I cannot help thinking that the fact that the Ombudsman's decision may give rise to a *res judicata* has profound implications so far as the scope of appellate review of such decisions are concerned. Where then - as in the present case - a complainant presents a complaint which might just as easily have been dealt with as a contractual claim within the court system and as the Ombudsman's resolution of this question will involve a binding adjudication which will in principle create a *res judicata*, it would seem to follow that the parties to the complaint are entitled to expect, at a minimum, that the ordinary principles of contract law will be correctly applied in the resolution of the dispute. If, by contrast, the Ombudsman's decision did not involve a binding adjudicatory decision and

was one which did not create a form of *res judicata*, then an entirely different approach to issues of deference and appellate review might well be justified.

15. The Ombudsman is, however, also entitled by virtue of the provisions of s. 57BK(4) to go further in order have regard to the substantive merits of the matter, even if this involves a departure from the strict rigours of contract law As I pointed out in *Koczan v. Financial Services Ombudsman* [2010] IEHC 407, the effect of s. 57BK(4) is, accordingly, that:

> "The Ombudsman's task, therefore, runs well beyond that of the resolution of contract disputes in the manner traditionally performed by the courts. It is clear from the terms of s. 57BK(4) that the Ombudsman must, utilising his or her specialist skill and expertise, resolve such complaints according to wider conceptions of *et aequo et bono* which go beyond the traditional limitations of the law of contract."

16. This is underscored by the provisions of s. 57CI(2) which, in effect, enables the Ombudsman to measure the general fairness of a contractual provision or action taken pursuant thereto by reference to general principles ("improper motive", "unjust", "unreasonable", "discriminatory" and so forth) which have been clearly transposed from the realm of public law and which would not ordinarily apply to a purely private contract. The powers which are conferred by both s. 57BK(4) and s. 57CI(2) of the 1942 Act are accordingly those which go far beyond the traditional boundaries of the law of contract. As I pointed out in *Koczan*, it is these particular novel powers which call for the application of the specialist skill and judgment of the Ombudsman so far as financial dealing is concerned and it is in this respect that the courts should show appropriate

deference to that specialist skill and judgment in the *application* of these wider principles to the facts of a given case.

17. This principle does not apply, however, so far as the ordinary application of the law of contract is concerned. It was never the intention of the Oireachtas that a complainant should be disadvantaged by electing to make a complaint to the Ombudsman rather than by proceeding in the ordinary courts. Within the judicial system no appellate court would hesitate to correct what it considered to be legal error on the part of the first instance court. The Supreme Court would not hesitate, for example, to reverse what it considered to be an erroneous decision of this Court on a point of contract law, no matter how experienced or expert the trial judge was in matters of contract or commercial law. In these circumstances, it could not be correct that this Court should defer to the Ombudsman on matters of pure contract law, not least given that the Ombudsman's decision would create a *res judicata* on that very contractual point which would bar the re-litigation of the issue before the ordinary courts.

18. Although both Mr. McDermott, counsel for the Ombudsman and Mr. White, counsel for Danske, urged that I should defer to the expertise of the Ombudsman on the question of the construction of the applicable contractual terms and conditions, it must be observed that the issue presented here involves the straightforward application of ordinary principles of contract law governing the construction of contractual documents. It follows, therefore, that for all the reasons which I have just advanced, it would be inappropriate for this Court to defer to the Ombudsman on these issues and thus only interfere if the interpretation of the contract which was arrived at was somehow unreasonable or irrational.

19. Moreover, just as it is clear that the courts will not defer to the views of specialist agencies on questions of statutory interpretation, the same must, in any event, be true in respect of purely legal questions of contractual construction. The former point was forcefully made by Barr J. in *Shannon Regional Fisheries Board v. An Bord Pleanála* [1994] 3 I.R. 449, 456:

> "Statutory interpretation is solely a matter for the courts and no other body has authority to usurp the power of the court in performing that function."

20. It follows, therefore, that the question of contractual construction is one which, generally speaking, at least, this Court is required to examine afresh in the course of determining a statutory appeal taken against a decision of the Ombudsman presenting such an issue.

The construction of clause 3

21. Turning now to that question, it will be seen that the key words are those contained in clause 3 ("…in response to market conditions…") of the applicable terms and condition. The Millars, while not contending for a form of tracker mortgage, argued nonetheless that the clause meant that the interest rates should generally follow general market conditions, *i.e.*, that the rate should decrease when rates were lowered generally, while accepting that the rate could increase when rates were generally increased. For its part, Danske contended that clause 3 did not refer to market conditions generally, but rather to its own cost of funding. It averred that as it did not avail of any ECB funding, the interest rates set by the ECB were not relevant to its own funding costs.

22. The Ombudsman concluded that clause 3 was "clear in its wording" and for this precise reason found against the Millars. I fear that I cannot agree. The term "market

conditions" is not a specialist term of art which has a defined meaning in legal or financial circles. Given that these words are not terms of art, they must therefore be construed in the first instance by reference to the ordinary usage of these terms and how, objectively, these words would be understood by a reasonable person in the context in which they appear.

23. In its more common usage the term "market conditions" may be taken to refer to "market conditions generally." While I agree that the term might also in some contexts refer to particular market conditions experienced, for example, by one undertaking in the relevant market, I should have thought that this was a less frequent usage. If, moreover, the construction urged by Danske were correct, it would mean that its interest rate could be varied by reference to special factors which were peculiarly within its own knowledge, the details of which it would not be obliged to disclose and which, as the Ombudsman himself acknowledged, the customer would have been obliged to accept more or less at face value. If this was, indeed, what was intended by the term "in response to market conditions", one might have supposed that more explicit language along these lines might have been used.

24. The clause is, in any event, an ambiguous one, the meaning of which falls to be determined by reference to the general factual background against which the contract was entered into: see generally *Analog Devices v. Zurich Insurance Co.* [2005] IESC 12, [2006] 1 I.R. 274, 280, *per* Geoghegan J. and the judgments of Fennelly and O'Donnell JJ. in *ICDL GCC Foundation v. European Computer Driving Licence Foundation Ltd.* [2012] IESC 12. In *Analog Devices* Geoghegan J. referred with approval to the judgment

of Lord Hoffmann in *Investor Compensation Scheme v. West Bromwich Building Society* [1998] 1 W.L.R. 866 in which the following principles of interpretation were set out:

> "(1) Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.
>
> (2) The background was famously referred to by Lord Wilberforce as the 'matrix of fact' but this phrase is, if anything, an understated description of what the background may include. Subject to the requirement that it should have been reasonably available to the parties and to the exception to be mentioned next, it includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man.
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> (3) The law excludes from the admissible background the previous negotiations of the parties and their declarations of subjective intent. They are admissible only in an action for rectification. The law makes this distinction for reasons of practical policy and, in this respect only, legal interpretation differs from the way we would interpret utterances in ordinary life. The boundaries of this exception are in some respects unclear. But this is not the occasion on which to explore them.
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> (4) The meaning which a document (or any other utterance) would convey to a reasonable man is not the same thing as the meaning of its words. The meaning of words is a matter of dictionaries and grammar; the meaning of the document is what the parties using those words against the relevant background would

reasonably have been understood to mean. The background may not merely enable the reasonable man to choose between the possible meaning of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must for whatever reason, have used the wrong words or syntax.....

(5) The 'rule' that words should be given their 'natural and ordinary meaning' reflects the commonsense proposition that we do not easily accept that people have made linguistic mistakes, particularly in formal documents. On the other hand, if one would nevertheless conclude from the background that something must have gone wrong with the language, the law does not require judges to attribute to the parties an intention which they plainly could not have had."

25. These principles were also expressly approved by the Supreme Court in *ICDL.* It follows, therefore, that having regard to the Lord Hoffmann's second principle, the Ombudsman could and should have had regard to the available background evidence in order to determine the precise meaning of this phrase in this particular context. That background evidence may - or may not - show that the words in question should have a more particular or a more general meaning. It is only where this background material cannot assist in resolving the ambiguity that, in line with the comments of O'Donnell J. (in his admittedly dissenting) judgment in *ICDL,* recourse should be had as a last resort to the principle of *contra preferentem.*

26. In any event, the Ombudsman would have been entitled, over and above the ordinary rules regarding the interpretation of contracts, to have regard to such relevant material to assist in ascertaining the objective intentions of the parties given that s. 57BK

empowers the Ombudsman to have regard to wider principles ("...the substantial merits of the complaint without regard to technicality or legal form...") which go beyond the strict confines of the substantive law of contract.

27. But even if the parties were to be confined to the ordinary law of contract and even if (contrary to my view) the term was not regarded as ambiguous, the Ombudsman would nonetheless have also been obliged to examine the question from a slightly wider perspective. If, for example, the Millars could establish that the definition of variable rate mortgage contained in Danske's website was one which was brought to their attention prior to entering into the contract, then they may – possibly - be able to establish by reference to sufficiently cogent evidence the existence of a collateral contract regarding the meaning of the term variable interest rate: see generally *Allied Irish Banks plc v. Galvin* [2011] IEHC 314, *Tennants Building Products Ltd. v. O'Connell* [2013] IEHC 197 and *Irish Bank Resolution Corporation v. McCaughey* [2014] IEHC 230. In other words, the Millars might be able to establish that they had been induced into entering these loan agreements by reference to a definition of variable rate mortgage contained in documentation supplied by Danske and from which Danske could not now in either law or in conscience be permitted to resile, even if that definition differed from the meaning ascribed to variable interest rate mortgage contained in clause 3. In that respect, the common law rules regarding collateral contracts have affinities with their equitable cousin, the doctrine of promissory estoppel.

Whether the Ombudsman's decision should be allowed to stand

28. In summary, therefore, the Ombudsman erred in concluding that the words ("...in response to market conditions....") in question were clear when they were not. He further

erred in not having regarding to the wider matrix of fact which, assessed objectively, might inform the meaning of these words as they appear in the relevant contractual documents. Nor did he give consideration to whether the Millars could successfully establish a collateral contract regarding the meaning of these words having regard to the promotional and other material supplied by Danske at the relevant time.

29. In any event, if the construction of clause 3 urged by Danske were to prove to be correct, the Ombudsman was nonetheless in error in failing to examine whether it would be broadly fair and reasonable for Danske to apply such a construction measured by reference to his enhanced statutory powers in s. 57BK(4) and s. 57CI(2): see, by analogy, my own reasoning on this very point in *Koczan.* In that case I held that the Ombudsman had erred in law in failing to analyse the automatic lapsing clauses provisions of an income protection policy by reference to these enhanced statutory powers. Just as in that case, I would emphasise that the application of these statutory powers calls for the application of the Ombudsman's particular expertise and nothing in this judgment is intended to express any view as to how these powers should be exercised in this case.

Conclusions

30. For all the reasons just stated, it is clear that, adopting the test articulated by Finnegan P. in *Ulster Bank v. Financial Services Ombudsman* [2006] IEHC 323, the decision reached by the Ombudsman "was vitiated by a serious and significant error or a series of such errors". It follows, therefore, that the Ombudsman's decision cannot be allowed to stand.

31. I will accordingly make an order pursuant to s. 57CM(2)(b) of the 1942 Act setting aside the decision of the Ombudsman of 10th December 2013. I will further make

an order pursuant to s. 57CM(2)(c) remitting the matter to the Ombudsman for a fresh determination of the complaint in a manner not inconsistent with this judgment.