DRN-1840716

Financial Ombudsman Service

The complaint

Mrs H has complained about the loans she took out with Skyline Direct Limited (Skyline). She says the loans were unaffordable.

What happened

Mrs H took 15 loans from Skyline between May 2013 and February 2016. Each of these loans was due to be repaid over a period 30 weeks. Some loans were repaid early. The last two loans are still outstanding. Some of the information Skyline provided about Mrs H's borrowing is shown below.

Loan	Date Taken	Date Repaid	Instalments	Amount	Repayment	Highest repayment
1	22/05/2013	04/12/2013	30	£400.00	£20.00	£20.00
2	07/08/2013	19/03/2014	30	£500.00	£25.00	£45.00
3	07/08/2013	12/02/2014	30	£500.00	£25.00	£70.00
4	12/02/2014	20/08/2014	30	£500.00	£25.00	£50.00
5	19/03/2014	20/08/2014	30	£300.00	£15.00	£40.00
6	25/07/2014	20/08/2014	30	£300.00	£15.00	£55.00
7	03/09/2014	18/02/2015	30	£500.00	£25.00	£25.00
8	22/10/2014	01/04/2015	30	£400.00	£20.00	£45.00
9	18/02/2015	27/05/2015	30	£500.00	£25.00	£45.00
10	15/04/2015	27/05/2015	30	£250.00	£13.00	£38.00
11	03/06/2015	11/11/2015	30	£500.00	£25.00	£25.00
12	15/07/2015	14/10/2015	30	£300.00	£15.00	£40.00
13	21/10/2015	06/01/2016	30	£500.00	£25.00	£50.00
14	09/12/2015	outstanding	30	£200.00	£10.00	£35.00

15	10/02/2016	outstanding	30	£700.00	£35.00	£45.00

* The “highest repayment” figure is sometimes made up of multiple payments and is the largest repayment Mrs H would have to make over the term of the loan.

Our adjudicator recommended Mrs H’s complaint be upheld from loans 6 onwards. She felt that the overall pattern of borrowing suggested Mrs H had become reliant on home credit loans.

I issued my provisional decision on 20 April 2020 upholding the complaint from loan 7 onwards. Mrs H accepted my provisional decision. Skyline did not accept my decision and provided new details of start and end dates of loans (which are shown in the table above).

The legal and regulatory framework and other publications

Skyline gave Mrs H loans 6 to 15 after the regulation of Consumer Credit Licensees had transferred from the OFT to the Financial Conduct Authority (“FCA”) on 1 April 2014. Skyline initially obtained interim permission to provide consumer credit before it went on to successfully apply for authorisation. Skyline’s interim permission to provide consumer credit and its eventual authorisation to do so meant that it was subject to the FCA rules and regulations from 1 April 2014.

The FCA’s Principles for Business set out the overarching requirements which all authorised firms are required to comply with. The Principles themselves are set out in PRIN 2.1.1R. And the most relevant principle here is PRIN 2.1.1 R (6) which says:

A firm must pay due regard to the interests of its customers and treat them fairly.

The FCA’s Consumer Credit sourcebook (CONC) is the specialist sourcebook for credit-related regulated activities. It sets out the rules and guidance specific to consumer credit providers, such as Skyline. CONC 5 sets out a firm’s obligations in relation to responsible lending. And CONC 6 sets out a firm’s obligations after a consumer has entered into a regulated agreement.

In its response to the view, Skyline has largely referred to CONC 5.2A and its subsections – but these rules are not relevant in this case as CONC 5.2A did not come in to force until November 2018.

The starting point for the relevant rules is Section 5.2.1R(2) of CONC which sets out what a lender needs to do before agreeing to give a consumer a loan of this type. It says a firm must consider:

(a) the potential for the commitments under the regulated credit agreement to adversely impact the customer’s financial situation, taking into account the information of which the firm is aware at the time the regulated credit agreement is to be made; and

(b) the ability of the customer to make repayments as they fall due over the life of the regulated credit agreement, or for such an agreement which is an open-end agreement, to make repayments within a reasonable period.

CONC also includes guidance about ‘proportionality of assessments’. CONC 5.2.4G(2) says:

A firm should consider what is appropriate in any particular circumstances dependent on, for example, the type and amount of credit being sought and the potential risks to the customer.

The risk of credit not being sustainable directly relates to the amount of credit granted and the total charge for credit relative to the customer's financial situation.

CONC 5.3 contains further guidance on what a lender should bear in mind when thinking about affordability. And CONC 5.3.1G(1) says:

In making the creditworthiness assessment or the assessment required by CONC 5.2.2R

(1), a firm should take into account more than assessing the customer's ability to repay the credit.

CONC 5.3.1G(2) then says:

The creditworthiness assessment and the assessment required by CONC 5.2.2R (1) should include the firm taking reasonable steps to assess the customer's ability to meet repayments

under a regulated credit agreement in a sustainable manner without the customer incurring financial difficulties or experiencing significant adverse consequences.

In respect of the need to double-check information disclosed by applicants, CONC 5.3.1G(4) states:

(b)it is not generally sufficient for a firm to rely solely for its assessment of the customer's income and expenditure on a statement of those matters made by the customer.

And CONC 5.3.7R says that:

A firm must not accept an application for credit under a regulated credit agreement where the firm knows or ought reasonably to suspect that the customer has not been truthful in completing the application in relation to information supplied by the customer relevant to the creditworthiness assessment or the assessment required by CONC 5.2.2R (1).

On 6 March 2019, The FCA wrote a '*Dear CEO'* letter to the Chief Executive Officer of all firms allocated to the 'High Cost Lenders' portfolio, which Skyline is part of. This letter was published sometime after Mrs H's agreements were entered into. But given that this letter didn't include any new rules and deals with how firms ought to be handling complaints about whether their previous lending was unaffordable, I do think that it offers some insight on the FCA's perspective on the rules. So I do consider it to be of some relevance in this case.

The letter set out the FCA's view of the key risks that High Cost Lenders pose to consumers and the markets they operate in. On page two of this letter, the FCA sets out its view of the key causes of harm. It says:

"To assess how firms in the High Cost Lenders portfolio could cause harm, we analysed their strategies and business models. We considered a wide range of information and data, including firms' regulatory histories, the number and nature of complaints, and findings from the HCCR. We also carried out diagnostic work on guarantor lenders, which involved issuing a data request to firms in October 2018.

Following our analysis, we see two key ways that consumers may be harmed across the High Cost Lenders portfolio:

- *a high volume of relending, which may be symptomatic of unsustainable lending patterns*
- *firms' affordability checks may be insufficient, leading to loans that customers may not be able to afford".*

The FCA sets out its areas of focus for all firms in the portfolio on page three of the letter. The section entitled 'Relending' says:

*"**Relending:** We have seen a high volume of relending across all credit products in the portfolio. We aim to carry out diagnostic work across the portfolio so that we can better understand the motivation for, and impact of, relending on both consumers and firms. This work will examine aspects of relending such as customers' borrowing journeys, firms' marketing strategies for offering additional credit and the costs of relending for consumers.*

We want to understand what harm, if any, relending may cause consumers. As part of this work, we will proactively engage with home-collected credit firms to ensure they understand our expectations. We will also discuss any changes to their processes as a result of the new rules and guidance on relending which we issued in our December 2018 Policy Statement on high-cost credit".

The section entitled 'Affordability' says:

***Affordability:** We recognise that there is an inherent challenge for these firms in assessing affordability for both new loans and repeat borrowing. High-cost credit customers' finances are often squeezed and they may have poor credit histories and low financial resilience. Nevertheless, firms must ensure that they are complying with all our affordability requirements. We gave an outline of these requirements in the Dear CEO letter we sent to HCSTC firms in October 2018. While this letter was aimed at HCSTC firms, the main principles are relevant to all firms in this portfolio.*

Finally, under the section entitled ***'Complaints'*** it says:

*"**Complaints:** We know that there have been increasing numbers of complaints about many of the products in this portfolio. Firms should ensure that they are handling complaints appropriately. We expect firms to fulfil all relevant obligations, including analysing the root causes of complaints and taking into account the Financial Ombudsman Service's relevant decisions. We gave further detail about what we expect from firms' complaint-handling procedures in the Dear CEO letter we issued to HCSTC firms in October 2018. This is equally relevant to all firms in the portfolio".*

Turning to the '*Dear CEO'* letter issued by the FCA on 15 October 2018, the third paragraph of this letter said:

"We note that the Ombudsman has recently published four examples of determinations of individual complaints about payday loans to illustrate its approach to the issues raised in those complaints (see: https://www.financial-ombudsman.org.uk/publications/technical.htm).

If relevant, firms should take these examples of determinations into account as part of establishing their own effective procedures for complaints handling (see DISP 1.3.1R)".

Paragraph eight of the letter went on to say:

"We would highlight in particular the risks in relation to repeat borrowing. These were flagged in our price cap proposals in CP14/10, in July 2014, in which we said that we were concerned that repeat borrowing could indicate a pattern of dependency on HCSTC that is harmful to the borrower. We noted that rigorous affordability assessments were key to avoiding harm in this area, and firms should ensure they are making responsible assessments of the sustainability of borrowing".

What I've decided – and why

I've considered Skyline's response to my provisional decision, along with all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

Whilst I haven't referred to all the points raised by Skyline below, I have considered them all and addressed those points that I consider material to the outcome of the complaint. That said; many of the points raised were already addressed in detail in my provisional decision.

Taking into account the relevant rules, guidance and law, I think the overarching questions I need to consider in deciding what's fair and reasonable in the circumstances of this complaint are:

- Did Skyline, each time it lent, complete reasonable and proportionate checks to satisfy itself that Mrs H would be able to repay in a sustainable way? If not, would those checks have shown that Mrs H would've been able to do so?
- Bearing in mind the circumstances, at the time of each application, was there a point where Skyline ought reasonably to have realised it was increasing Mrs H's indebtedness in a way that was unsustainable or otherwise harmful and so shouldn't have provided further loans?
- Did Skyline act unfairly or unreasonably in some other way?

If I determine that Skyline did not act fairly and reasonably in its dealings with Mrs H and that she has lost out as a result, I will go on to consider what is fair compensation.

Did Skyline, each time it lent, complete reasonable and proportionate checks to satisfy itself that Mrs H would be able to repay in a sustainable way?

It is important to note that the FCA didn't, and doesn't, specify exactly how an assessment of affordability is to be carried out but the *"extent and scope"* and the *"types and sources of information to use"* needed to be enough to be able to reasonably assess the sustainability of the arrangement for the consumer.

In other words, the assessment needs to be consumer-focussed. It is not an assessment of the risk to the lender of not recovering the credit but of the risk to the consumer of incurring financial difficulties or experiencing significant adverse consequence as a result of the decision to lend.

As set out in CONC, the risk to the consumer directly relates to the particulars of the lending and the circumstances of the consumer. Therefore, a lender's assessment of creditworthiness would likely need to be flexible. That is to say, what is sufficient for one consumer might not be for another, or indeed what might be sufficient for a consumer in one circumstance might not be so for the same consumer in other circumstances.

Bearing the above in mind, I would expect an assessment of creditworthiness to vary with circumstance. In general, I'd expect a lender to require more assurance, the greater the potential risk to the consumer of not being able to repay the credit in a sustainable way.

Certain factors might point to the fact that Skyline should fairly and reasonably have done more to establish that any lending was sustainable for the consumer. These factors include, *but are not limited to*:

- the *lower* a customer's income (reflecting that it could be more difficult to repay a given loan amount from a lower level of income);

- the *higher* the amount due to be repaid (reflecting that it could be more difficult to meet a higher repayment from a particular level of income);

- the *longer* the term of the loan (reflecting the fact that the total cost of the credit is likely to be greater and the customer is required to make payments for an extended period); and

- the *greater* the number and frequency of loans, and the *longer* the period of time during which a customer has been given loans (reflecting the risk that ongoing use of these loans may signal that the borrowing had become, or was becoming, unsustainable).

Skyline considers its checks were proportionate. It told us that as part of the affordability assessment, its representative visited the customer's home (having obtained permission with 24 hours' notice) and carried out a detailed income and expenditure assessment. It referred any previous payment history to identify any significant risk indicators. It also completed a pre-contract process, which included the amount of money the customer received, the amount to be repaid and the number and value of repayments, as well as a completed loan agreement. Skyline said Mrs H had to confirm and sign the various documents.

Skyline has provided some information about what Mrs H's declared about her income and expenses from loan 9 onwards. I haven't seen that information for loans 6-8, but in any event, I think Skyline should have been doing more than what it told us it did do at least by the time Mrs H took out loan 6. To be clear, I don't think the checks it did from loan 9 onwards were enough either.

By this point Skyline should have done more than rely on the information Mrs H was providing about her finances. I think it should have taken steps at that time to have verified Mrs H's true financial position.

Skyline already had an established lending history with Mrs H by the time it provided loan 6. In these circumstances I think Skyline's checks for loan 6 (as well as the subsequent ones) ought to have built upon what it clearly knew about Mrs H from her earlier borrowing. That is to say, to remain proportionate, Skyline's affordability checks needed to evolve and take into account what it was learning as a result of earlier applications.

I also think that Mrs H's borrowing history itself suggested there was a reasonable prospect the information she provided was inaccurate. For example, on loan 9 (the first loan where I can see it asked for Mrs H's income and expenses) I think it ought to have been apparent to Skyline that Mrs H did not really have a weekly disposable income of £255. if it had been it seems unlikely she would need to borrow a loan that amounted to less than two weeks' disposable income? And, in these circumstances, I think that Skyline ought to have taken steps to verify the accuracy of the information.

Skyline will also be aware that while Mrs H did sign the declarations, it shouldn't have proceeded with loan applications where it ought reasonably to have suspected that the information provided was inaccurate. And, in this case, I think that Skyline also ought to have questioned just why it was Mrs H wanted or needed a seventh, eighth, ninth, tenth loan and beyond – at very high interest rates - if she genuinely had the levels of disposable income declared. Given Skyline's obligations, I consider it fair, reasonable and proportionate for it to have taken further steps to ascertain that this genuinely was the case, by the time of loan 6 and for the subsequent ones. It could have done this independently or by asking Mrs H to provide supporting evidence such as payslips, utility bills, or bank statements. I don't think Skyline's checks achieved this.

I say this while also mindful of the fact that the various rules and regulations in place at the time Skyline was lending to Mrs H also make it clear that where income and expenditure is used in an affordability assessment, it may not be proportionate to rely solely on a statement of these matters made by the borrower.

To help us understand for ourselves what Skyline would more likely than not have discovered if it had completed reasonable and proportionate checks before providing these loans, we would normally ask Mrs H for her bank statements. But Mrs H does not have any bank statements. However, I don't think I need to recreate individual, proportionate affordability checks for loans 6 to 15 in this case.

Bearing in mind the circumstances, at the time of each application, was there a point where Skyline ought reasonably to have realised it was increasing Mrs H's indebtedness in a way that was unsustainable or otherwise harmful and so shouldn't have provided further loans?

In addition to assessing the circumstances behind each *individual* loan provided to Mrs H by Skyline, I also think it's fair and reasonable to look at the *overall pattern* of lending and what unfolded during the course of Mrs H's lending history with Skyline. This is because, there may come a point where the lending history and pattern of lending itself demonstrates that the lending was unsustainable.

Looking at the relevant rules and guidance as summarised in the earlier part of my decision, Skyline was required to establish whether Mrs H could sustainably repay her loans – not just whether the loan payments were affordable on a strict pounds and pence calculation.

The loan payments being affordable on this basis *might* be an indication a consumer could sustainably make their repayments. But it doesn't automatically follow this is the case. Similarly, repaying a loan early does not automatically mean the consumer is repaying the loan in a sustainable way. This is because CONC defines sustainable as being without undue difficulties and in particular the customer should be able to make repayments on time, while meeting other reasonable commitments; as well as without having to borrow to meet the repayments.

It follows that a lender should realise, or it ought fairly and reasonably to realise, that a borrower won't be able to make their repayments sustainably if they're unlikely to be able to make their repayments without borrowing further.

The adjudicator considered this point was reached by loan 6. I explained why in my provisional decision I didn't agree. I said in my provisional decision that there were some warning signs that Skyline ought to have been alert to but I don't think that Skyline ought to have concluded that the pattern of lending had, in itself, become demonstrably unsustainable or harmful – such that I could reasonably say that the facts spoke for themselves by loan 6. I explained that this was because the lending and highest repayment

(taking into account any overlapping loans) had actually decreased when loans 5 and 6 were taken out when compared to earlier loans.

However, I reached this conclusion based on the facts about the start and end dates of the loans I had before me at the time. Since then Skyline has provided start and dates which contradict this conclusion.

For this reason, I have reviewed my decision. Given the particular circumstances of Mrs H's case and the new information that has come to light, I think that this point was reached by loan 6. I say this because:

- At this point Skyline ought to have realised Mrs H was not managing to repay her loans sustainably. Mrs H had taken out 6 loans within 14 months and Mrs H had been continuously indebted to Skyline for the entire time. Bearing in mind Mrs H's initial loan should have been repaid over 30 weeks (just over 6 months) and her indebtedness to Skyline should, to all intent and purpose, have been discharged at this point, Skyline ought to have realised there was a strong possibility Mrs H was having to borrow further to cover the hole her loan payments was leaving in her finances and that Mrs H's indebtedness may have been increasing unsustainably.

- Mrs H's first loan was for £400 and loan 6 was for £300 but was taken out whilst loans 4 (for £500) and 5 (for £300) were still outstanding. At this stage, Mrs H's weekly payment was almost three times what it was for loan 1. It was the second highest payment* she had made and the second time she had three overlapping loans. At this point Skyline ought to have known that Mrs H was not likely borrowing to meet a temporary shortfall in her income but to meet an ongoing need.

- From loan 6 onwards Mrs H was provided with a new loan whilst still having previous loans outstanding. There was a 14 day between loan 6 and 7 but I don't consider this gap to be significant. There would not have been many (if any) pay cycles during this time. It is important to note that the overall lending had already been going on for almost 16 months by this point.

- Mrs H wasn't making any real inroads to the amount she owed Skyline. Loan 15 was taken out nearly three years after Mrs H's first. And it was for a larger amount. Mrs H had paid large amounts of interest to, in effect, service a debt (which had increased) to Skyline over an extended period.

*I note loan 3 had a higher weekly payment (when looking at overlapping loans 1 and 2) but this was very early on in the lending relationship, so I don't think that Skyline ought to have concluded that the pattern of lending had, in itself, become demonstrably unsustainable or harmful at this point.

Skyline has referred to the FCA's High-cost Credit Review (CP 18/43) and whilst the review highlighted that those who use home credit over longer period do not appear to suffer significant harm in the same way as other parts of the high cost credit markets, it does not follow that users of home credit never suffer any financial distress. Indeed, the review also highlights that:

'*there are existing controls that reduce the risk of unaffordable debt and financial distress. These include that:*

- *Firms must assess creditworthiness (including affordability) before agreeing any new loan, or any significant increase in credit.*

- *Firms also have to monitor consumers' repayment patterns to identify signs of financial distress. They must take appropriate action where there are signs of actual or possible repayment difficulties.*

- *Firms must also not encourage a customer to refinance where the commitments are not sustainable or are not in the customer's best interests, or do so without the customer's consent/request.*

I've already explained, in some detail, in this decision why I think that Skyline's creditworthiness assessments weren't fair, reasonable and proportionate and therefore weren't effective.

And the consultation paper CP 18/12 section 3.14 states that

"*we are concerned that there is a small core of customers who are using home-collected credit over an extended period and that some customers are being unduly influenced by firms' representatives to keep borrowing*."

So, while I acknowledge that the FCA has said that repeat lending won't always lead to an unfair outcome for consumers, I don't think that the FCA's publications support the assumption that repeat lending (where home-collected credit is concerned) will always be fair reasonable and proportionate in all circumstances.

It is worth adding that while I don't consider that my findings are inconsistent with the content of the FCA's publications, I am, in any event, required to decide what I think is fair and reasonable in the particular circumstances of Mrs H's case.

In this particular case, Mrs H was in debt to Skyline for almost three years. This lack of any real breaks in Mrs H's indebtedness leads me to think that it ought to have been apparent to Skyline that Mrs H was unlikely to have been using these loans as a useful means of managing cyclical income shortfalls – especially as the loan amounts and total repayments across overlapping loans increased substantially by the end of the relationship.

Mrs H's pattern of consistently settling loans with funds from later ones was indicative of a customer whose debt had become unsustainable. And Skyline continuing to provide Mrs H with loans in this way, meant that she was paying Skyline high amounts of interest for the privilege of it allowing her to continue to delay dealing with her unsustainable debt.

Did Skyline act unfairly or unreasonably in some other way?

I've thought about everything provided. Having done so, I've not seen anything here that leads me to conclude Skyline acted unfairly or unreasonably towards Mrs H in some other way.

Did Mrs H lose out as a result of Skyline's shortcomings in relation to the loans from loan 6 onwards?

I think that Mrs H suffered adverse consequences as a result of Skyline unfairly giving her loans 6 to 15. I say this because:

- These loans had the effect of unfairly prolonging Mrs H's indebtedness to Skyline by allowing her to take very expensive credit over an unbroken and extended period of

time and the financial loss arising (by way of interest and charges on loans she shouldn’t have been given) has unfairly exacerbated what was already an adverse and precarious financial position for Mrs H.

- The number of loans and length of time they were taken over is likely to have had implications for Mrs H’s ability to access mainstream credit. The greater the presence of these loans on Mrs H’s credit file the less likely Mrs H was able to rehabilitate her finances and regain access to mainstream credit.

Fair compensation – what Skyline needs to do to put things right for Mrs H

Skyline shouldn’t have given Mrs H loans 6-15. To put things right Skyline should:

A. add together the total of the repayments made by Mrs H towards interest, fees and charges on these loans.

B. calculate 8% simple interest* on the individual payments made by Mrs H which were considered as part of A calculated from the date Mrs H originally made the payments, to the date the complaint is settled.

C. Skyline may if it chooses to use the total of A plus B to repay any principal which it has written-off. Mrs H was unable to repay loans 14 and 15 in full.

D. Pay any remaining refund to Mrs H. If there is no refund left and still a balance outstanding made up of written-off principal, it would not be fair for Skyline to pursue this further.

E. The overall pattern of Mrs H's borrowing for loans 6-15 means any information recorded about them is adverse, so Skyline should remove these loans entirely from Mrs H's credit file.

*HM Revenue & Customs requires Skyline to deduct tax from this interest. Skyline should give Mrs H a certificate showing how much tax it has deducted, if she asks for one.

My final decision

For the reasons I’ve explained above and in my provisional decision, I’m partially upholding Mrs H’s complaint and direct Skyline Direct Limited (Skyline) to pay compensation as set out above.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mrs H to accept or reject my decision before 19 June 2020.

Kathryn Milne
Ombudsman