

The complaint

Mrs N complains that Studio Retail Limited (“Studio Retail”) irresponsibly increased the credit limit on a catalogue shopping account and continued to allow her to borrow when it should have been clear she was facing financial difficulties.

What happened

Mrs N opened a catalogue shopping account with Studio Retail in March 2017. At that time her credit limit was initially set at £100. The credit limit was increased a number of times, reaching £1,100 in March 2019 before being increased for a final time in October 2019 when the credit limit was set at £1,400. Studio Retail then reduced the limit to £970 in July 2020, that it says was due to arrears on the account. Mrs N defaulted on her repayments in the same month and the debt was sold on by Studio Retail in October 2020 to a third party.

Mrs N’s complaint has been assessed by one of our adjudicators. He didn’t think that Studio Retail had done anything wrong initially. But he thought that by the time the credit limit was increased to £1,100 in March 2019, Studio Retail should have seen that Mrs N might be facing problems repaying what he owed. So, he didn’t think that credit limit increase should have been agreed. And he thought that by September 2019, Studio Retail should have taken steps to freeze Mrs N’s account as it should have realised the credit was no longer suitable for him. So, our adjudicator asked Studio Retail to put things right for Mrs N.

Studio Retail has disagreed with our adjudicator’s view and thinks it has done nothing wrong at any stage it agreed to lend to Mrs N. It says based on what it had in front of it, that Mrs N was managing her accounts well and there was nothing to show that she was having problems with her finances, up to the point she started getting into arrears and it then reduced her credit limit.

So, as the complaint hasn’t been resolved informally, it has been passed to me, an ombudsman, to decide. This is the last stage of our process. If Mrs N accepts my decision it is legally binding on both parties.

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.

We’ve set out our approach to unaffordable/irresponsible lending complaints on our website and I’ve kept this in mind while deciding Mrs N’s complaint.

The rules and regulations at the time required Studio Retail to carry out a reasonable and proportionate assessment of whether Mrs N could afford to repay what she owed in a sustainable manner. This assessment is sometimes referred to as an “affordability assessment” or “affordability check”. The check needed to be completed at the outset of the relationship and each time there was a significant increase in the credit limit. Studio Retail also needed to monitor the account for any signs that Mrs N was struggling to manage the credit she’d been given.

The checks had to be “borrower” focused – so Studio Retail had to think about whether repaying the credit sustainably would cause difficulties or adverse consequences for Mrs N. In practice this meant that Studio Retail had to ensure that making the required repayments wouldn’t cause Mrs N undue difficulty or adverse consequences. In other words, it wasn’t enough for Studio Retail to simply think about the likelihood of it getting its money back, it had to consider the impact of any repayments on Mrs N.

Checks also had to be “proportionate” to the specific circumstances at that time. In general, what constitutes a proportionate affordability check will be dependent upon a number of factors including – but not limited to – the particular circumstances of the consumer (e.g. their financial history, current situation and outlook, and any indications of vulnerability or financial difficulty) and the amount / type / cost of credit they are seeking.

In light of this, I think that a reasonable and proportionate check ought generally to have been *more* thorough:

the *lower* a customer’s income (reflecting that it could be more difficult to make any repayments to credit from a lower level of income);

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

the *longer* the period of time a borrower will be, or has been, indebted for (reflecting the fact that the total cost of the credit is likely to be greater and the customer is required to make repayments for an extended period).

There may also be other factors which could influence how detailed a proportionate check should’ve been for a given application – including (but not limited to) any indications of borrower vulnerability and any foreseeable changes in future circumstances. I’ve kept all of this in mind when thinking about whether Studio Retail did what it needed to before agreeing to open an account for Mrs N, and to agree the subsequent increases to her credit limit.

Studio Retail has told us that it set, and managed, Mrs N’s credit limit by reference to information it received from a credit reference agency, and by looking at how Mrs N was managing her credit account. But although Studio Retail has very recently given us summary information about some of these checks, it hasn’t given us any detail about the results it received on each occasion that it increased her credit limit.

The credit limit Studio Retail agreed when the account was first opened was relatively small - I don’t think it would’ve been proportionate for Studio Retail to ask Mrs N for the amount of information that would be needed to show the lending was unsustainable before opening the account. So, I don’t think the original lending decision should cause me any great concerns. And I think the same applies to the increases to the credit limit that took place during 2017. During that time Mrs N appears to have operated her account relatively well, maintaining its balance within the agreed credit limit, and making the required repayments on time.

In May 2018, the credit increase that Studio Retail applied remained relatively modest. And given the smooth operation of the account to that time I don’t think that it would be reasonable to expect Studio Retail to have gathered the additional it might have needed to identify any problems that Mrs N was facing. I think that its checks remained proportionate and that overall, they showed there was no reason for it to not increase Mrs N’s credit limit.

Towards the end of 2018, Mrs N’s outstanding balance increased to around £500. In March 2019 the balance on account was around the same, and with this, Studio Retail increased

the credit limit to £1,100. By then Mrs N had held the account for nearly two years and although there were times when she had repaid some of the balance on the account, at no time had she been successful in repaying all that she owed. I think that ought to have been of increasing concern to Studio Retail. It needed to do more than just check whether Mrs N could afford to repay what she owed when it increased her credit limit. It also needed to monitor her use of the credit facility over its lifetime. So, although Mrs N was operating her account relatively well, and making all her contractual repayments, I don't think that Studio Retail had any reasonable grounds to conclude that a further increase in Mrs N's credit limit would be appropriate at this stage.

In October 2019 when it increased Mrs N's credit limit further, Mrs N had still not made any inroads to the balance on the account that she had accrued since December 2018 and by this stage she had held the account open for around 29 months. So, on balance, based on what I have just concluded, I don't think that it was reasonable for Studio Retail to increase Mrs N's credit limit in October 2019 either.

The repayments Mrs N had been able to make from December 2018 had little effect in reducing her outstanding balance. So, I think by September 2019 Studio Retail should have reached the point where it accepted Mrs N was facing problems managing her money. It should have treated her at that point with forbearance and with due consideration. I think an appropriate response would have been to prevent Mrs N from making any further purchases using the account and to stop the addition of any new interest.

So, in summary, I don't think Studio Retail should have increased Mrs N's credit limit in March 2019 and it follows, October 2019 also. And I think that by September 2019 it should have stopped her taking any further credit and suspended the addition of interest to the account. So, Studio Retail needs to put things right for Mrs N.

Putting things right

To put things right, Studio Retail should reconstruct Mrs N's account by making the following adjustments;

I don't think Studio Retail should have agreed to increase Mrs N's credit limit in March 2019. So, Studio Retail should remove any interest incurred on amounts from the date of increase in March 2019 onwards. It follows that this also includes the credit increase in October 2019.

I don't think Studio Retail should have agreed to allow any further purchases to be made using the account from September 2019. So, Studio Retail should remove any interest and charges (including delivery fees, Buy Now Pay Later interest, and PPP insurance premiums) added to the account after 1 September 2019.

Studio Retail should remove any adverse information recorded on Mrs N's credit file that wouldn't have been added if the above adjustments had been applied at the time.

If, after making these adjustments, Mrs N's account was in credit at any time, Studio Retail should pay Mrs N interest at a rate of 8% simple* on the credit balance for the period it is in credit.

If a credit balance remains at the end of the calculations Studio Retail should refund that amount to Mrs N, adding interest at a rate of 8% simple* on the credit balance to the date of settlement.

* HM Revenue & Customs requires Studio Retail to take off tax from this interest. Studio Retail must give Mrs N a certificate showing how much tax it's taken off if she asks for one.

My final decision

My final decision is that I uphold part of Mrs N's complaint. I direct Studio Retail Limited to put things right as I have described above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs N to accept or reject my decision before 6 September 2021.

Mark Richardson
Ombudsman