

The complaint

Mr A complains that Black Horse Limited mishandled the rejection of a car, he'd acquired under a hire purchase agreement, which had been of unsatisfactory quality.

What happened

In July 2018, Mr A entered into a four-year hire purchase agreement for a new car. As part of the agreement to take the new car, Mr A part-exchanged his current car. However, the price paid by the dealership didn't clear the outstanding balance on the credit agreement for that car, leaving Mr A with £8,927 in negative equity to clear.

Mr A paid £3,000 to the dealership, which was put towards clearing the negative equity. This left £5,927 outstanding from the original credit agreement to clear.

The manufacturer paid the dealership a "*Finance Dealership Allowance*" of £2,669, to put towards the cost of Mr A's new car.

The hire purchase agreement was drawn up. It showed the price of the goods as the cost of the car and the remaining outstanding negative equity combined, which was £60,477. It then recorded that there had been a deposit of £2,669, which had reduced the amount of credit to £57,808. The agreement set out the total hire purchase charges that would be added to credit amount, the cost of the monthly instalments Mr A was to pay, and the final lump sum instalment Mr A would need to pay at the end of the agreement, should he wish to keep the car. This lump sum was equal to the guaranteed future value of the car.

Mr A says that he found the car was faulty within a short time of acquiring it. He says he experienced intermittent problems with the car's engine, software and lights. The car was inspected and repaired by the dealership.

In July 2019, Mr A remained unhappy about the quality of the car and complained to Black Horse, who offered him £150 as compensation for dealing with a faulty car. Mr A disagreed with the amount of compensation offered by Black Horse and complained to this service.

During our investigation Mr A supplied further evidence to Black Horse that the car continued to have faults, in particular with its infotainment system. In December 2019, Black Horse agreed that the car wasn't of satisfactory quality, and that Mr A was entitled to reject it and cancel the credit agreement. As Mr A had driven 27,000 miles, since he'd acquired the car, Black Horse said that it was fair that he paid something towards the usage.

Black Horse offered the following redress to Mr A:

- £1,230 as a part refund of his direct debits plus interest
- £500 compensation for the distress and inconvenience caused
- Reimbursement of around 25% of the payments he'd made under the agreement to reflect the loss of enjoyment of using car that had faults.

Total redress = £4,887.

However, Black Horse said that there remained negative equity to clear of £5,927, arising from the other agreement. So, to end this hire purchase agreement, Black Horse said that it would put the redress towards clearing that outstanding amount and Mr A would need to pay the remaining £1,039 to clear the negative equity from the first credit agreement.

Mr A was unhappy at the charges imposed by Black Horse and asked our investigator to look at this part of his complaint.

Our investigator recommended that Mr A's complaint should be upheld and said that Black Horse had acted unfairly when calculating the amount to be reimbursed to Mr A. He said that it would be fair for Black Horse to have also paid Mr A the £2,669 that had been put toward the car, even though this hadn't been a sum paid by him.

However, our investigator said he felt the refund, compensation and reimbursement for loss of enjoyment had been fairly applied. But Black Horse should have also taken into account the amount that had been paid towards the new agreement by the manufacturer and Mr A, which was a total of £5,669. This amount had been set against the full amount owing under the agreement, which covered both the car and the negative equity.

Looking at the amount Mr A had paid towards this agreement, our investigator said this amounted, one way or another, to £11,596 but the negative equity had actually been £8,927. So, it would be fair for him to receive back the £2,669.

Mr A agreed with our investigator's view, but Black Horse disagreed. It said that the manufacturer's contribution was widely accepted as not being a deposit that was returnable to a consumer, as they had not paid it. This allowance had been paid not by the dealership but by the manufacturer, as an incentive to new customers to reduce the amount of credit needed to purchase a new car. The purpose of the allowance wasn't to clear a customer's outstanding debt.

Black Horse said that, if there hadn't been any negative equity owing by Mr A, and the agreement had been cancelled in the same circumstances, then this allowance wouldn't be considered as something that should be reimbursed to Mr A.

As the parties weren't able to agree the complaint was passed to me. I issued a provisional decision along the following lines.

While I appreciated the Financial and Leasing Association's non-binding guidance on negative equity was issued after this hire purchase agreement had been set up, I thought it was helpful when looking at whether this credit agreement was fair in relation to Mr A paying for the car and clearing the negative equity. This guidance set out that where there was a hire purchase agreement for a car, together with negative equity on a previous agreement, then the hire purchase element should be distinct from the refinancing of the negative equity. This was because the hire purchase had to be linked to the hire of the vehicle in question, and not the refinancing of an existing debt. There should be two separate agreements for each of the elements. Care should also be taken to explain to the consumer the nature of the agreements and, if it wasn't, then there may be an impact in its enforceability.

Here, the outstanding negative equity had been added to the cost of the car, so there weren't two separate agreements for each of the sums. As the negative equity element

wasn't distinct from the cost of the car, I thought it was confusing for Mr A as to what he was paying off with each of his monthly instalments. For instance, do all of the payments go to clearing the cost of the car first and then later to clear the negative equity or vice versa. The terms of the agreement didn't set out how they payments were to be attributed to the two separate elements. So, as these amounts had been combined, I thought it would be fair to treat each of Mr A's monthly instalments as going towards clearing both the cost of the car and the negative equity.

As it wasn't disputed that the car was of unsatisfactory quality, I wasn't going to look at that, so the issue for me was whether Black Horse had acted fairly in the way it had handled the settlement of Mr A's account.

It also wasn't disputed that, when Mr A had part-exchanged his first car for the new one, there had been an outstanding balance owed by Mr A, as the amount the dealership paid for the car wasn't sufficient to settle the credit agreement. This negative equity had been settled by Black Horse as part of the agreement for the new car. I also thought it was fair to say Mr A knew that there was an outstanding amount on his original agreement

I'd seen that the full amount of the negative equity was £8,927. Mr A had made a payment of £3,000 to the dealership, which Black Horse said had been paid to reduce this negative equity. I'd seen that this amount wasn't included in either the hire purchase agreement, nor in the new car's invoice. So, I thought it was more likely than not that Mr A understood this sum wasn't going towards the purchase cost of the new car. I thought it was fair that Black Horse had used that sum towards the settling of Mr A's previous credit agreement. And I wasn't going to ask Black Horse to reimburse Mr A this amount.

Looking at the £2,669 Finance Dealership Allowance, I'd seen this was a separate incentive paid by the manufacturer towards a credit agreement taken out for a new car. I accepted this amount wasn't paid by Mr A and, therefore, he wouldn't suffer a financial detriment if this amount wasn't awarded to him.

I disagreed with the approach taken by our investigator that this amount should have counted towards the negative equity, as that wasn't its purpose. I agreed with Black Horse that, had this credit agreement not had the element of negative equity, then it would be a very unusual requirement for the business to reimburse a manufacturer's contribution to a consumer if the agreement was later cancelled and rewound. So, I wasn't going to ask Black Horse to reimburse this amount.

However, as I'd set out above, I didn't think this hire purchase agreement set out clearly that there were two elements being paid by Mr A, and this wasn't fair. I thought it would be reasonable to consider that Mr A had been paying towards the negative equity, as well as the car, so I didn't think Black Horse should have treated the full amount of the negative equity as being outstanding when the agreement was cancelled.

Mr A had paid around 21 months, out of a total of 48 due instalments, at the point the agreement was cancelled. As I thought it was fair to assume that the negative equity did not form any part of the guaranteed future value of the car, I also thought it was fair to say that the negative equity would have been cleared in full before the final optional payment fell due in the 49th month.

Taking into account the amount that was credited back to Mr A by Black Horse as it was accepted he was entitled to reject the faulty car, I thought, in the circumstances, it would now be fair to treat Mr A as though he had cleared one third of the amount of the negative equity. I had reduced the number of months paid (21/48) because Black Horse hadn't

considered the negative equity element of the payments when it calculated what would be a fair reimbursement to Mr A. And I thought it would be fair to now add that element into the calculation. Adjusting the reimbursement provided by Black Horse and taking the number of months Mr A had paid under the agreement, I thought it was fair to find that Mr A owed £3,915, and not £5,927 for the negative equity, so there were two thirds of the negative equity remaining.

Black Horse offered a settlement to Mr A that took account of his spoiled enjoyment of the car, by reimbursing him 25% of his instalments, a refund of around a further two months' instalments and £500 compensation. Looking at the use Mr A has had of the car, I agreed that a full refund of all of his instalments wouldn't be reasonable. I thought the approach taken by Black Horse, in these circumstances, was fair though this should have been 25% of the portion of his monthly instalment that went to paying the cost of the car.

I also thought that it was fair to require Mr A to clear the negative equity from the original agreement. Though as stated above, I thought Black Horse's calculation as to what that amount was hadn't been fair. I thought only £3,915 should have been considered as outstanding, and to put things right, anything paid by Mr A over this amount should now be reimbursed to him.

So, I intended to uphold Mr A's complaint. I understood Mr A had paid Black Horse the requested £1,039 to close the account meaning that he had now in effect paid £5,927 to clear the negative equity. And I was therefore intending to ask Black Horse to reimburse him £2,012 which was the amount he had overpaid, as the negative equity figure should have been treated as £3,915 at the point when the agreement was cancelled. I thought it would also be fair for this amount to be paid with interest from the date of payment until the date of settlement

Mr A says that although he had hoped for a slightly different outcome, he thinks the decision is fair for the reasons I've given. Black Horse says that the decision is unfair as it only deducted a cost for Mr A using the car from the reimbursement it made of his monthly instalments. This deduction equated to 45p per mile and the money retained was therefore only to cover use and nothing else.

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 have looked carefully at my provisional decision and I haven't changed my mind. I still think the way the hire purchase agreement failed to make clear how Mr A was clearing the negative equity element was unfair. I think it's reasonable to consider that each of the monthly payments made by Mr A went towards both the negative equity and the cost of the car. I also think it's fair to assume Mr A had that expectation too.

I've seen that Mr A made use of the car before it was agreed he could hand it back due to its inherent fault. And I think Black Horse has acted fairly in making a deduction for that use. It says that it charged him 45p per mile which has worked out as the equivalent of 75% of each of his monthly instalments. However, when using the 45p per mile charge I don't think that Black Horse took into account that a proportion of each of the monthly instalments was paying off the negative equity. So, I can't say Black Horse looked at all the circumstances when deciding whether or not that amount to charge for use was fair.

I think it would have been fairer if, rather than applying 45p per mile, Black Horse had used a percentage of the monthly instalment to cover use. This would have allowed it to take into

account both that it had recognised Mr A had suffered a loss of enjoyment using the car and also that not all of the monthly instalment was being paid towards its cost.

So, I still think it's fair and reasonable to treat Mr A as though he had paid off one third of the negative equity. This takes into account the number of payments he had made before the agreement was ended and that there should be a deduction for usage he'd made of the car.

For the reasons given above, I'm upholding Mr A's complaint

Putting things right

I'm asking Black Horse Limited to reimburse Mr A £2,012 together with interest at the yearly rate of 8% simple from the date of payment until the date of settlement.

My final decision

As set out above, I'm upholding Mr A's complaint. I'm asking Black Horse Limited to reimburse Mr A £2,012 together with interest at the yearly rate of 8% simple from the date of payment until the date of settlement.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr A to accept or reject my decision before 26 April 2021.

Jocelyn Griffith
Ombudsman