Financial Ombudsman Service

Complaint

Mrs F has complained that Zopa Limited ("Zopa") unfairly arranged unaffordable guarantor loans for her. She says any checks would have shown that she couldn't afford to repay what she was being lent.

Background

Zopa operated the electronic system in relation to lending which led to Mrs F being provided with a first loan in April 2018. The loan was for £3,000.00 and due to be repaid in 36 monthly instalments of £105.90. Mrs F settled this loan early with some of the proceeds from a second loan for £10,000.00 which Zopa arranged in October 2018.

Loan 2 was due to be arranged in 48 monthly instalments of £287.05. Finally, Zopa arranged a third loan for £11,500.00 in May 2019 and some of the proceeds from this settled the second loan. This loan was due to be repaid in 60 monthly instalments of £310.54.

Mrs F's complaint was reviewed by one of our adjudicators. He thought that Zopa hadn't acted unfairly when bringing about loan one. However he also thought that Zopa ought to have seen that Mrs F wasn't in a position to repay loans 2 and 3 at the time it arranged them. So he partially upheld Mrs F's complaint.

Zopa disagreed with our adjudicator's view but Mrs F didn't. Zopa said that it was happy its check were completed in line with the regulator's rules and so it didn't think it had done anything wrong when bringing about these loans. As Zopa disagreed with our adjudicator, the complaint was passed to an ombudsman for a final decision.

As the parties are no longer in dispute over loan 1, this final decision is only considering whether Zopa acted fairly and reasonably towards Mrs F when it brought about loans 2 and 3.

My findings

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 general approach to complaints about unaffordable/irresponsible lending - including the key rules, guidance and good industry practice - on our website. And I've referred to this when deciding Mrs F's complaint.

Having carefully thought about everything, I think that there are two overarching questions that I need to answer in order to fairly and reasonably decide Mrs F's complaint.

These two overarching questions are:

- Did Zopa complete reasonable and proportionate checks to satisfy itself that Mrs F would be able to meet her obligations under the P2P agreements in a sustainable way?
    - If so, did it make a fair decision?
    - If not, would those checks have shown that Mrs F would've been able to do so?
- Did Zopa act unfairly or unreasonably in some other way?

If I determine that Zopa didn't act fairly and reasonably in its dealings with Mrs F and that she has lost out as a result, I will go on to consider what is fair compensation.

Did Zopa complete reasonable and proportionate checks to satisfy itself that Mrs F would be able to meet her obligations under the P2P agreements in a sustainable way?

The rules, regulations and good industry practice in place when Zopa brought about these P2P agreements with Mrs F required it to carry out a proportionate assessment of whether she could afford to make her repayments. This assessment is sometimes referred to as an "affordability assessment" or "affordability check".

The checks had to be "borrower" focused – so Zopa had to think about whether repaying the loan sustainably would cause difficulties or adverse consequences *for Mrs F*. In practice this meant that Zopa had to ensure that making the payments to these loans wouldn't cause Mrs F undue difficulty or significant adverse consequences. In other words, it wasn't enough for Zopa to simply think about the likelihood of Mrs F making payments, it had to consider the impact of loan repayments on Mrs F.

Checks also had to be "proportionate" to the specific circumstances of the application. 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. Even for the same customer, a proportionate check could look different for different applications.

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 loan repayments to 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 repeated refinancing may signal that the borrowing had become, or was becoming, unsustainable).

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 carefully thought about all of the relevant factors in this case.

Were Zopa's checks reasonable and proportionate?

Zopa has said that it completed an income and expenditure assessment with Mrs F before arranging these loans. It says also carried out credit checks to work out what Mrs F's existing credit commitments were too.

I've carefully thought about what Zopa has provided and what it has said about its checks. But given the credit check for loan two showed some adverse information and that Mrs F had taken out additional borrowing since loan 1, and Mrs F was returning for substantially more in funds, I think Zopa's checks ought to have gone further. In my view, Zopa needed to do more to get a better understanding of just why it was she wanted further funds when she already appeared to be quite heavily indebted. And it follows that I think Zopa ought to have found out more about Mrs F's circumstances when she returned for even more funds for loan 3, only a few months later.

Indeed, it seems to me that Zopa merely carried out the same checks for all three of Mrs F's loans. And think that this led to Zopa failing to take into account the whole picture of its overall lending history with Mrs F, in favour of a narrower focus on the individual applications, which presented a more favourable picture of a deteriorating position.

Given Zopa's own information showed that Mrs F's debt to income ratio was increasing, I would have expected it to have taken further steps to verify Mrs F's income and expenditure to ensure she had the necessary funds to repay the loan it was arranging.

As Zopa proceeded with loans 2 and 3 in circumstances where Mrs F's indebtedness was increasing without taking steps to verify her income and expenditure, I'm satisfied that the checks Zopa carried out before arranging these loans weren't reasonable and proportionate.

<u>*Would reasonable and proportionate checks have indicated to Zopa that Mrs F would have been unable to repay these loans?*</u>

As reasonable and proportionate checks weren't carried out before these loans were provided, I can't say for sure what they would've shown. So I need to decide whether it is more likely than not that proportionate checks would have told Zopa that Mrs F would've been unable to sustainably repay these loans.

Mrs F has now provided us with evidence of her financial circumstances at the time she applied for these loans. Of course, I accept different checks might show different things. And just because something shows up in the information Mrs F has provided, it doesn't mean it would've shown up in any checks Zopa might've carried out.

But in the absence of anything else from Zopa showing what this information would have shown, I think it's perfectly fair, reasonable and proportionate to place considerable weight on it as an indication of what Mrs F's financial circumstances were more likely than not to have been at the time.

Having reviewed the Zopa's income and expenditure assessment for loan 2, I can see that Zopa's own calculations confirmed that Mrs F had just under £500 left over once her rent and monthly credit commitments were deducted from her income. Zopa's own assessment therefore shows that Mrs F would have been left with around £200 a month after all the credit and rent commitments and the payments to this loan were met.

However, Mrs F would be required to meet all her essential living and transportation costs from this £200 a month. The information Mrs F has provided shows that her living costs were substantially in excess of £200 a month. In fact, when Mrs F's food, transportation costs (which Zopa ought to have been aware of) and other non-credit related commitments are taken into account, her essential living and transportation costs were closer to £500. Given these were commitments Mrs F would be expected to make over the course of loan 2, it follows that the monthly payments to loan 2 were unaffordable.

Given the short period between loans 2 and 3, unsurprisingly, Mrs F's essential living and transportation costs were pretty similar at the time of loan 3. And as Mrs F would be required to make payments of just over £300 as well as her essential living and transportation costs from around £725 a month, it follows the payments to loan 3 were also unaffordable.

Bearing all of this in mind, I'm satisfied reasonable and proportionate checks would more likely than not have demonstrated that Mrs F would not have been able to make the repayments to loans 2 and 3.

Did Zopa act unfairly or unreasonably towards Mrs F in some other way?

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

So I find that Zopa didn't act unfairly or unreasonably towards Mrs F in some other way.

Conclusions

Overall and having carefully thought about the three overarching questions, set out on pages one and two of this decision, I find that Zopa:

- *didn't* complete proportionate checks on Mrs F to satisfy itself that she was able to repay loans 2 and 3;
- reasonable and proportionate checks *would* more likely than not have shown Mrs F was unable to make the repayments for loans 2 and 3 without borrowing further or suffering significant adverse consequences;
- Zopa *didn't* also act unfairly or unreasonably towards Mrs F in some other way.

The above findings leave me concluding that Zopa unfairly and unreasonably brought about loans 2 and 3 for Mrs F in October 2018 and May 2019.

Did Mrs F lose out as a result of Zopa unfairly and unreasonably bringing about her loans?

I think that these loans had the effect of unfairly increasing Mrs F's indebtedness as it led to her to being given additional credit she couldn't afford to repay. The monthly payments, which also included interest and charges, took up a reasonable portion of Mrs F's income at a time where she was already struggling to make ends meet.

So I find that Mrs F did suffer significant adverse consequences and as a result lost out because Zopa unfairly arranged these loans.

Fair compensation – What Zopa needs to do to put things right for Mrs F

Having considered everything, I think it is fair and reasonable for Zopa to put things right for Mrs F in the following way:

- refund all the interest, fees and charges Mrs F paid on loan 2;

- removing all interest, fees and charges applied to loan 3 from the outset. The payments made should be deducted from the new starting balance – the £11,500.00 originally lent. Zopa should treat any payments made should the new starting balance be cleared as overpayments. And any overpayments should be refunded to Mrs F. If an outstanding balance remains on loan 3 after these adjustments, Zopa can use the compensation due for loan 2 to reduce and clear this balance.

- add interest at 8% per year simple on any interest, fees, charges and overpayments from the date they were paid by Mrs F to the date of settlement†;

- remove any adverse information recorded on Mrs F's credit file as a result of loan 2. Any adverse information recorded about loan 3 should also be removed in the event Mrs F no longer has an outstanding balance with Zopa, once all adjustments have been made.

† HM Revenue & Customs requires Zopa to take off tax from this interest. Zopa must give Mrs F a certificate showing how much tax it has taken off if she asks for one.

If after all of the above adjustments have been made (including offsetting the compensation for loan 2) an outstanding balance remains on loan 3, Zopa should set up an affordable payment plan for Mrs F. I'd also remind Zopa of its obligation to exercise forbearance if it intends to collect on an outstanding balance, should one remain after all adjustments have been made to the account, and it's the case that Mrs F is experiencing financial difficulty.

My final decision

For the reasons I've explained, I'm upholding Mrs F's complaint. Zopa Limited should put things right for Mrs F in the way I've set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs F to accept or reject my decision before 11 October 2021.

Jeshen Narayanan
Ombudsman