DRN-2865515

The complaint

Miss T says UK Credit Limited lent to her irresponsibly.

What happened

Miss T took out a 36-month guarantor loan for £2,000 from UK Credit on 20 November 2014. This means it was given on the basis Miss T had a guarantor who would be responsible for making the repayments if she failed to. The monthly repayment was £95.94 and the total repayable was £3,453.84.

Miss T says proper affordability checks were not carried out.

Our investigator found the complaint should be upheld. He said based on what it saw during its checks UK Credit ought to have realised it was likely the loan would not be sustainably affordable for Miss T.

UK Credit disagreed. In summary, it said the investigator was assuming someone with bad credit will always have difficulty with credit. It had asked Miss T about the adverse information on her credit file and it was due to unexpected circumstances. Its affordability assessment, which considered the cost of repaying both defaulted and active debt, showed Miss T would have surplus income each month after taking on this loan. Miss T only struggled with her repayments due to further unexpected circumstances, and not due to the affordability of the loan.

UK Credit asked for an ombudsman to review the complaint, so it was passed to me.

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.

Our approach to unaffordable/irresponsible lending complaints is set out on our website and I've followed it here.

The regulations, rules and guidance that were in place when UK Credit lent to Miss T obliged UK Credit to lend responsibly. Amongst other things, UK Credit was required to carry out a reasonable and proportionate assessment of whether Miss T could afford to repay what she owed in a sustainable manner. This is sometimes referred to as an affordability assessment or an affordability check.

The checks also had to be borrower-focused. So UK Credit had to think about whether repaying the credit sustainably would cause any difficulties or adverse consequences for Miss T. In other words, it wasn't enough for UK Credit to simply think about the likelihood of it getting its money back, it had to consider the impact of the loan repayments on Miss T.

Checks also had to be proportionate to the specific circumstances of each loan application. In general, what makes up a proportionate affordability check will be dependent upon a number of factors including – but not limited to – the particular circumstances of the consumer (eg. their financial history, current situation and outlook, and any indications of vulnerability or financial difficulty) and the amount, type and cost of credit they have applied for. 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 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 UK Credit did what it needed to before agreeing to lend to Miss T, and have considered the following questions:

- did UK Credit complete reasonable and proportionate checks when assessing Miss T's loan application to satisfy itself that she would be able to repay the loan in a sustainable way?
- if not, what would reasonable and proportionate checks have shown?
- did UK Credit make a fair lending decision?
- did UK Credit act unfairly or unreasonably in some other way?

UK Credit asked for some information from Miss T before it approved the loan. It asked for details of her income and verified this with a payslip and tax credits letter. It asked about her living costs and noted she was solely responsible for these and had two dependents. It checked her credit file to understand her credit history and her existing credit commitments. It discussed the adverse data on her file with her to understand the reasons. It asked about the purpose of the loan - it was for Christmas expenses. From these checks combined UK Credit concluded Miss T would be left with monthly disposable income of £166.32 and so the loan was affordable.

I think the checks UK Credit carried out were proportionate, but I am not persuaded it made a fair lending decision based on the information it gathered. I'll explain why.

The credit check UK Credit carried out showed that Miss T had defaulted on eight accounts between March 2011 and October 2014. She seemed to be making token payments on some, but not all of these accounts. And three of these defaults were registered in the month prior to this loan application. From this I think UK Credit ought to have realised Miss T was having problems managing her money. It argues that we cannot assume bad credit means a person will always have difficulty with credit. I would agree, but three new defaults in the month prior to a loan application is not historic adverse data – it was a very recent indication that Miss T was unable to prevent three accounts defaulting, even if the arrears had started some time ago. I think this is clear evidence she was not stable financially.

UK Credit argues that an unexpected event caused the defaults. I have listened carefully to the security call when it asked about all the defaults. Miss T actually says she'd had 'a bad few months' explaining it was because she'd had 'a couple of days off sick' and so didn't get paid. I don't think it was responsible for UK Credit to accept that as an explanation given the number of defaults it saw on Miss T's credit file. It also argues that a more recent credit check shows Miss T has since reduced the amount of defaulted debt she owes to £260 and has improved her credit. But I am not persuaded this is a fair or comprehensive analysis – that same report shows her overall indebtedness increased seven fold and she had two County Court Judgments registered against her in that same time period.

In addition, UK Credit only accounted for £20 per month for all Miss T's credit commitments in its affordability assessment. When the investigator flagged this it recalculated them to be £60.59. The investigator argued they were higher when the full credit limit on Miss T's active credit was taken into account. Either way, even using UK Credit's revised calculation which would leave Miss T with around £120 of surplus income, I think in the circumstances of this case the lender ought to have been concerned.

Miss T was on a relatively low income and had two dependents, and there were recent adverse entries on her credit file. I think if UK Credit had taken a borrower-focused approach it would have allocated a buffer to cover unplanned costs – particularly given some of Miss T's declared expenses were very low eg. £10 a month on clothing for 1 adult and 2 young children. And had it done so I don't think it could have fairly concluded Miss T would have been left with sufficient disposable income. The problems Miss T went on to have making repayments were largely triggered by what UK Credit describes as unexpected circumstances. But I think had it better scrutinised the data it gathered it ought to have realised there was a risk this loan would not be sustainably affordable for Miss T, given her recent financial instability, personal circumstances and lack of any contingency in her expenditure.

It follows I think UK Credit was wrong to lend to Miss T.

I have not seen any evidence UK Credit acted unfairly or unreasonable towards Miss T in some other way.

Putting things right

It's reasonable for Miss T to have repaid the capital amount that she borrowed as she had the benefit of that money. But she has paid interest and charges on loans that shouldn't have been given to her. So she has lost out and UK Credit needs to put things right.

It should:

- Refund all interest and charges. Add up the total amount Miss T repaid and deduct the sum from the capital amount.
- If reworking Miss T's loan accounts results in her having effectively made payments above the original capital borrowed, then UK Credit should refund these overpayments with 8% simple interest calculated on the overpayments, from the date the overpayments would have arisen, to the date of settlement*.
- If reworking Miss T's loan accounts results in an outstanding capital balance, UK Credit should try to agree an affordable repayment plan with Miss T.
- Remove any adverse information recorded on Miss T's credit file in relation to the loan.

*HM Revenue & Customs requires UK Credit to deduct tax from this interest. UK Credit should give Miss T a certificate showing how much tax it's deducted, if she asks for one.

My final decision

I am upholding Miss T's complaint. UK Credit Limited must put things right as set out above.

Under the rules of the Financial Ombudsman Service, I’m required to ask Miss T to accept or reject my decision before 19 April 2022.

Rebecca Connelley
Ombudsman