

The complaint

Mr W is unhappy that Tesco Personal Finance PLC, trading as Tesco Bank ("Tesco"), provided him a loan after falling victim to a fraud.

What happened

In 2016, Mr W fell victim to an elaborate and sophisticated investment fraud. Mr W had invested a large amount of money in a so-called binary options investment company. But when he attempted to release some of his equity, he was informed that he wasn't able to do so until he'd reached a certain level of investment.

Mr W informed the fraudster that he didn't have any further funds to invest. It was at this point that the fraudster suggested taking out a loan in order to make up the remaining amount required to draw his investment. Mr W says that he didn't have any other choice, other than to lose his investment. So, he agreed to go ahead with the loan.

Mr W says that he was too busy to apply for the loan. So, the fraudster suggested that they contact Tesco on Mr W's behalf, which he agreed to. The fraudster took the relevant information required for the loan from Mr W and applied for a personal loan of £23,500. The loan was approved and paid into a bank account held in Mr W's name. On 26 September 2016, Mr W transferred £23,423 to the fraudsters from his bank account where the loan had been received.

The fraudster continued to deceive Mr W by informing him that the loan payment hadn't been received. Mr W continued to send money to the fraudster that he'd loaned from a family member. But eventually the requests became unreasonable to Mr W and he realised the company wasn't legitimate and he had in fact been defrauded.

Mr W reported the fraud to Tesco, but it told him it couldn't raise a fraud claim as he'd admitted to signing and agreeing to the loan. He continued to make payments on the account until 2020 where he approached our service to look into things again.

Tesco looked into Mr W's concerns but didn't think it'd made an error. It said that as Mr W had agreed to the loan and the funds were paid into his personal bank account, it couldn't be held responsible for any subsequent payments made to a third-party.

Mr W remained unhappy with Tesco's response, so an Investigator at our service looked into his concerns again. After reviewing the evidence, the Investigator disagreed with Tesco and recommended that the complaint be upheld.

In summary, they thought Tesco's affordability and creditworthiness checks weren't sufficient. And had sufficient checks been carried out, they thought Tesco likely would have

uncovered the incorrect information held on the application and, ultimately, the fraud.

They recommended Tesco write off the loan, return any repayments to Mr W including interest, remove any reporting of the loan from Mr W's credit file and pay £300 in compensation for the impact of the error.

Tesco disagreed with the recommendations. It highlighted the following reasons:

- The application was completed online, and sufficient verification checks were carried out on the information provided using Credit Reference Agencies (CRAs) to ensure the application was genuine.
- The credit agreement was posted to Mr W's genuine address and he agreed to this by signing and returning it.
- The loan was paid into Mr W's genuine account. It wasn't until this point that Mr W decided to transfer the loan to a third-party.
- It felt it adhered to the regulatory requirements when carrying out proportionate affordability checks and didn't feel further checks were warranted due to Mr W's good credit history and low risk score.
- Nothing in the application form indicated vulnerability or an attempt to defraud it.
- It felt that it couldn't be held responsible for any loss as it didn't have control over how Mr W chose to spend the loan.

As Tesco disagreed with the Investigator's assessment, the matter was passed to me for a decision.

On 8 March 2022 I issued provisional findings to both parties asking for any further comments and evidence by 22 March 2022. My provisional findings were as follows:

'When considering what is, in my opinion, fair and reasonable, I've taken into account relevant law and regulations; regulator's rules, guidance and standards; codes of practice; and what I believe to have been good industry practice at the relevant time.'

Affordability

There are two key questions I need to consider in order to decide what's fair and reasonable in the affordability circumstances of this complaint. These questions are:

- 1. Did Tesco complete reasonable and proportionate checks to satisfy itself that Mr W would be able to repay the borrowing in a sustainable way?*
 - a. If so, did it make a fair lending decision?*
 - b. If not, would reasonable and proportionate checks have shown that Mr W could sustainably repay the borrowing?*
- 2. Did Tesco act unfairly or unreasonably in some other way?*

Tesco's obligations at the time are set out in the FCA's Consumer Credit sourcebook (CONC). Amongst other things, this sets out that assessments should be carried out to establish the creditworthiness of a customer prior to lending.

In short, CONC 5.2.3 says that the extent of any creditworthiness assessment should be dependent upon, and proportionate to, a number of factors. Some of these factors include:

- *The amount of credit*

- *The financial position of the customer at the time of seeking the credit*
- *The customer's existing financial commitments including mortgages*

CONC 5.3.1 goes on to say that if income and expenditure is taken into account in its creditworthiness assessment, it is not generally sufficient to rely upon a statement of those matters made by the customer.

In the circumstances of this complaint, Tesco has supplied the information provided on the loan application form. This sets out basic information such as Mr W's personal information including employment status, monthly income, residential status, repayments on existing debt and the purpose of the loan. Mr W has confirmed that some of the information set out in the application is incorrect. This includes:

- *He was self-employed rather than full time employed*
- *His salary was inflated considerably*
- *He wasn't taking the loan out for 'home improvements'*

Tesco has said that it fulfilled its obligation to carry out affordability and due diligence checks by running the information provided in the application through credit reference agencies (CRAs), which is an independent source. This satisfied it that the information provided matched Mr W's and that he could afford the loan repayments. It was also satisfied that

Mr W had applied for the loan as it was being paid into an account in his name and the credit agreement was delivered to his genuine address, signed and returned.

Other than the checks carried out via CRAs, Tesco has confirmed that it didn't perform any other checks, such as on Mr W's employment status or income and regular monthly expenditure, which wouldn't have been provided through CRA checks.

As I've already touched upon, CONC says that checks have to be "proportionate" to the specific circumstances of the loan application. What constitutes a proportionate affordability check will be dependent upon a number of factors including, but not limited to, the circumstances of the borrower and the amount, type and cost of credit they are seeking. In light of this, a reasonable and proportionate check ought generally to have been more thorough:

- *The lower a customer's income*
- *The higher the amount due to be repaid*
- *The longer the term of the loan*

In the circumstances of this complaint, it appears that Tesco took some of the information provided at face value, such as Mr W's income and employment status.

The checks Tesco were required to carry out had to be 'borrower focused'. So instead of seeing how statistically likely Mr W was to repay the borrowing, it needed to assess whether he could sustainably repay the borrowing, taking into account his personal circumstances.

And it needed to base its creditworthiness assessment on sufficient information. So, I think the checks needed to take into account Mr W's personal circumstances.

In this case, Mr W had to pay back £23,500 over ten years with monthly repayments of £299.94. So, I think this was a significant commitment.

Tesco has supplied a copy of the credit assessment it undertook. This gave summaries of Mr W's credit commitments with a total balance of £98,133 – the majority of which was a mortgage, which had a balance of £91,000. Tesco has recorded this as a joint mortgage and halved the monthly repayment commitment from £306 to £153. However, having looked at Mr W's credit report, there is no indication that the mortgage was joint and shows Mr W's repayments as £306.

The credit search also shows Mr W had a loan with a balance of £7,133 and payments of around £200 per month.

Tesco also estimated Mr W's monthly living expenses as £320 based upon statistical information rather than information supplied by Mr W himself.

I've also considered that the loan application contained Mr W's employment status as 'full time employed' but listed the name of the company he was employed with as containing his own surname, which could have been an indicator that it was in fact his own company and he was in fact self-employed. And as I've highlighted above, the rules state that it's not generally acceptable when taking into account a customer income and expenditure to rely upon a statement made by the customer on those matters.

Mr W has told our service that he was receiving an average salary of £1,252 in the three months prior to the loan application. This was significantly lower than that claimed on the application form by the fraudster. And Mr W was unaware of this fact as he'd not filled out the application and didn't receive a copy of the information contained within it.

Tesco has made submissions that even based upon this income, Mr W would have been approved for the loan. But based on its own calculations, it'd predicted Mr W's outgoings as £653. Adding the loan repayments applied for, this would have increased Mr W's estimated expenditure to £958, bringing it very close to his total monthly income. I think this would have presented an additional concern to Tesco.

Considering all the above factors, I'm minded to find that the checks carried out by Tesco weren't sufficient to satisfy its requirements under CONC. This is particularly so when considering the loan amount, term of repayment and repayment amount.

Would reasonable and proportionate checks have indicated to Tesco that Mr W would have been unable to repay the loan?

Mr W has provided us with his bank statements from around the time he applied for the agreement. These provide some detail about his income and expenditure. I appreciate different checks show different things, and Tesco may have chosen to look at something else, but I think these are fair for me to consider when weighing up Mr W's financial circumstances at the time he entered into the agreement.

These statements corroborate Mr W's salary as being, on average, £1,252 per month. It also shows that Mr W had a committed monthly expenditure of approximately £1000.

This left Mr W with approximately £260 for other expenditure. And when considering that the repayments for the debt applied for required monthly repayments higher than £260, this loan was unaffordable to Mr W.

Could Tesco have identified and prevented the fraud?

Having reviewed the evidence provided by both parties, I'm minded to come to a different view of that expressed in the Investigator's assessment.

While I've highlighted in my provisional findings that Tesco's affordability checks weren't proportionate and the loan was unaffordable, I don't think it would have been obvious to it that Mr W had fallen victim to a fraud.

Additional affordability or creditworthiness checks likely would have resulted in Tesco asking Mr W to provide additional information to prove his monthly expenditure and monthly salary. And while this would have shown that he couldn't afford the repayments of the loan, it likely wouldn't have revealed the circumstances in which he was applying for it.

Mr W was aware that the loan was being applied for. He willingly provided his personal information to a third-party to allow them to apply for the loan on his behalf and admits signing and returning the credit agreement.

The evidence that Mr W likely would have provided to Tesco would have likely resulted in it ultimately rejecting the application rather than it contacting him to question the discrepancies. So, I don't think Tesco were provided with an opportunity to identify the fraud. It knew Mr W was receiving the funds into his own bank account. It had also confirmed his identity via CRA checks and by sending the credit agreement to his genuine home address and had this returned signed. I don't think this presented sufficient suspicion surrounding the circumstances of the application to reasonably suspect a third-party's involvement and question it.

In addition to this, Mr W should bear some responsibility in allowing a relatively untrusted third-party permission to apply for the loan on his behalf. And I don't think he checked that the information within that application was accurate and true before signing and returning the credit agreement associated with it.

Ultimately, Mr W did give permission for the application to be made by the third-party. And he did receive the funds associated with that loan to his genuine bank account. I appreciate and empathise with the fact that he didn't receive the benefit of these funds, as he transferred them onto the fraudster. But I don't think it's fair or reasonable to hold Tesco liable for this loss.

For the above reasons, I don't think it's fair to hold Tesco liable for the principle sum of the loan amount.'

I concluded that I was minded to uphold the complaint and direct Tesco to:

1. Refund all interest, fees and charges Mr W has paid on the loan adding 8% simple annual interest from the date they were paid to the date of settlement.
2. Remove all interest, fees and charges applied to the loan from the outset.
3. Remove any adverse reporting of the debt from Mr W's credit file.

Mr W's response

Mr W said that his main assertion in this matter was that a crime had been committed. He

felt that it was inappropriate that Tesco desired to be the inadvertent beneficiary of the crime.

He asked that a more favourable compromise be considered and that his monthly repayments end rather than him paying for being a victim of crime.

He further added that he thought there was a drive to stamp out this type of crime rather than prologing it.

Tesco's response

Tesco remained of the opinion that its original lending decision was correct. It repeated some of the obligations set out in CONC that I'd highlighted in my provisional findings and said that its checks were proportionate. It said:

- Whether income verification checks were needed or not is risk based as it would be impractical to verify every last customer.
- It was unaware of any way to verify the employment status or loan purpose for every customer.
- The application set out that Mr W was full-time employed. Had it known Mr W was self-employed, and had been for less than two years, it would have verified his income.
- It would only "refer" a customer if the value of the loan was over a certain threshold, which was not met.
- The length of the loan was 10 years, which is the maximum allowed. Based on Mr W's declared income and age at the end of the loan term, it had no reason to be concerned.

Now that both parties have responded to the findings set out in my provisional decision, I'm now ready to issue my final decision.

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.

Taking into account the responses to my provisional findings, I don't intent to depart from the findings made. I've set out in the provisional decision why I was minded to conclude the way in which I did. So, I don't intent to repeat these points again in my final decision. But I will address some of the concerns raised by both parties.

Mr W's response

Mr W has highlighted that a crime has been committed against him and that this is his main assertion. But Tesco, nor I, have denied this point.

I'm empathetic to Mr W's circumstances, and that he's been victim to a callous fraud. But the person responsible for the fraud committed against him is ultimately the fraudster themselves. It wouldn't be fair or reasonable to hold financial businesses liable for the losses of all victims of crime unless a business failed in its legal, regulatory or good industry practice obligations to protect the customer and prevent the loss.

As I've set out in my provisional decision, I don't think Tesco did fail to identify and prevent the fraud from taking placed. So, it wouldn't be reasonable to hold it liable for the loss.

I'd also like to point out to Mr W that my findings concluded that Tesco should remove any interest and charges from the loan. This means that Mr W would only be paying back the principle sum owed. This means that Tesco wouldn't be making a profit from the loan, only getting the money back that it sent to him.

Tesco's response

Tesco has reiterated a number of points it'd already raised with our service prior to the issuing of my provisional findings. But there are some additional points that I'd like to address.

Tesco says that it's not aware of any way that it can verify a customer's employment status or purpose for the loan. But this wasn't specifically highlighted as an expectation in the findings I issued. My findings set out that the affordability assessment wasn't proportionate to the amount, term and repayments of the loan—all of which were substantial.

As I've already highlighted, some of the information relied upon was either taken at face value from the application or cross referenced using electronic bureau data rather than verified. I think it would have been prudent to take additional steps to verify the information provided given the above factors. Had proportionate checks been carried out here, it's clear that Mr W wouldn't have been approved the loan.

Tesco has also pointed out in its response that it would be impractical to verify all of a customer's information on every application. But I've not said that it should do this in every application. To the contrary, carrying out the same checks in every case isn't proportionate.

I remain of the opinion that proportionate checks weren't carried out here. And I think had they been done, it would have been clear to Tesco that Mr W couldn't afford the loan repayments.

Putting things right

As recommended in my provisional decision, Tesco should refund Mr W any interest and charges he's already paid on the account. It should also remove any remaining interest and charges and reporting of the debt to Mr W's credit report.

Mr W will however be required to repay the principle sum loaned to him. Mr W can contact Tesco to arrange how best to pay this amount.

My final decision

For the reasons I've given above, I uphold this complaint against Tesco Personal Finance PLC and direct it to:

- Refund all interest, fees and charges Mr W has paid on the loan adding 8% simple annual interest from the date they were paid to the date of settlement.
- Remove all outstanding interest, fees and charges applied to the loan.
- Remove any adverse reporting of the debt from Mr W's credit file.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr W to accept or reject my decision before 25 April 2022.

Stephen Westlake
Ombudsman