DRN-3326322

The complaint

Mrs L complains that Tesco Personal Finance PLC trading as Tesco Bank ("Tesco") lent irresponsibly when they approved her loan.

What happened

In May 2015, Mrs L applied for a loan of £18,500 over a term of four years with Tesco. The loan was approved and included an initial payment holiday so that the first repayment of £438.23 wasn't due until September 2015.

Mrs L maintained repayments until December 2017, when she contacted Tesco to advise them of a change in her circumstances. Her working hours had been reduced and she was struggling to maintain her contractual payments. Tesco agreed a reduced payment plan of £220 a month for six months.

In May 2018, Mrs L contacted Tesco again. She said she couldn't maintain the agreed repayments and couldn't clear her arrears. Tesco reviewed Mrs L's income and expenditure and agreed a further payment reduction to £60 a month for six months. Tesco also sent a default notice to Mrs L and made formal demand for what she owed.

In October 2018, Mrs L contacted Tesco as she had reduced her working hours further due to ill health. Tesco reviewed her income and expenditure again which showed her surplus income had reduced by £200 a month. Tesco agree a payment plan of £10 a month for 12 months. Tesco passed control of Mrs L's loan to a debt collection agency in March 2019.

In October 2021, having sought impartial advice about her loans and debt, Mrs L realised that the loan provided by Tesco was unaffordable at the time given her other financial commitments. Mrs L believes that had Tesco properly checked her credit record, this would've shown she had late payments and defaults together with other outstanding credit. She thought Tesco had lent irresponsibly, so complained to them.

Tesco didn't agree they'd lent irresponsibly. They said their decision was based on the information provided by Mrs L together with other checks they carried out. They said they were not obliged to verify Mrs L's income and relied upon the information Mrs L provided.

Mrs L wasn't happy with Tesco's response, so she referred her complaint to this service. Having considered all the information and evidence, our investigator agreed that Tesco's decision to lend here was unaffordable. Our investigator thought the level of disposable income calculated by Tesco was proportionally low and meant Mrs L was unlikely to have been able to sustainably make her repayments.

Tesco didn't agree with our investigator's findings. They said that when calculating Mrs L's disposable income, they considered Office for National Statistics (ONS) data which take's account of general cost of living expenses. Tesco said Mrs L's credit file showed her as a low credit risk and they'd used verified data to calculate whether the loan was affordable. They also said that Mrs L's financial difficulties resulted from a change in her circumstances that they couldn't predict.

As an agreement couldn't be reached, Mrs L's complaint has been passed to me to consider.

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.

The rules and guidance relevant at the time Tesco provided Mrs L with the loan were set by the Financial Conduct Authority (FCA) in the Consumer Credit Sourcebook (CONC). These required Tesco to carry out an assessment using reasonable and proportionate checks to determine whether Mrs L could afford to repay the loan in a sustainable way. Those checks needed to be borrower focussed and consider whether making the repayments could result in financial difficulties for Mrs L.

This service believes that any checks needed to consider Mrs L's personal circumstances and would usually need to be more thorough:

- the lower a consumer's income; and
- the higher the amount due to be repaid; and
- the longer the term of the loan; and
- the greater the number and frequency of loans.

Conversely, a less detailed affordability assessment, without the need for verification, is far more likely to be fair, reasonable, and proportionate where the amount to be repaid is relatively small, the financial situation is stable, and the debt is for a relatively short period.

Tesco have provided details of the information used to assess Mrs L's loan application. Mrs L stated her net monthly income as £1,400 with a monthly mortgage commitment of £200. Her application detailed no other commitments or outgoings. The credit reference and bureau information obtained by Tesco showed no evidence of delinquent accounts, arrears within the previous six months, or defaults. But the searches did reveal that Mrs L had unsecured debts totalling £18,790 and existing debt repayments of £395 a month, in addition to her mortgage. It also showed there was either a notice of correction or a dispute in existence. Tesco assumed living expenses totalling £320 a month based upon ONS data. I don't think it's unreasonable to use this information. Their assessment suggested that Mrs L had a monthly surplus of £47 after paying these commitments together with the required repayment on her new loan.

While Tesco's checks may suggest Mrs L could afford the repayments on the proposed new loan, I think there was sufficient to suggest that additional checks and assessments were required. I say this because there were clear differences between the information in Mrs L's application, and the data received from the credit bureaus. In particular, relating to Mrs L's existing finance commitments.

The proposed new loan (including interest), together with the existing unsecured debt revealed, meant that Mrs L's total indebtedness would increase to almost £40,000, including interest. This is almost 2.4 times her stated net annual income. In addition, the monthly surplus calculated by Tesco of £47 equated to a very small proportion of her net monthly income. So, I think it's reasonable to conclude that a relatively small change in Mrs L's financial circumstances could've resulted in her repayments becoming unsustainable.

So, with that conclusion, had Tesco undertaken further checks and tests, would this have resulted in a different outcome? Mrs L's application states that the loan was for home improvements. But she's confirmed it was actually to consolidate existing debts that she'd accrued. Further, Mrs L says she'd recently raised a mortgage to repay other debts at the time. I appreciate that Mrs L didn't provide this information when she applied, but this does raise questions about Mrs L's financial situation at the time.

While I've considered Tesco's response to our investigator's findings, I think there was enough to prompt them to have undertaken more detailed tests and checks and questioned the information provided by Mrs L. And had they, I'm not persuaded that a responsible lender would've reasonably concluded that the new loan was sustainably affordable. So, I agree that Tesco's decision to lend here doesn't feel appropriate.

Putting things right

Ultimately, it's always difficult to put someone back in the position they would've been had a loan not been given. The money has been lent and Mrs L has benefited from that. So, I think it's fair that Mrs L pays back what she's spent. But I don't think it would be fair or reasonable to expect Mrs L to incur any costs associated with the loan. So, I will be asking Tesco to refund all interest, fees and charges from the point the money was first lent.

In the event that the refund of charges, fees and interest results in a balance being due to Mrs L (i.e. where there's been overpayments), Tesco should pay 8% simple interest from the date of each overpayment to the date of settlement. If there remains an outstanding debt, Tesco should ensure an affordable repayment plan is agreed.

Mrs L has asked for all associated adverse information reported to be removed from her credit file. I agree that my decision needs to be reflected in what's reported to the credit reference agencies. But equally, it's important that other potential lenders are aware of Mrs L's existing commitments and difficulties, including any amount she may still owe to Tesco. So, I think the fairest way to put that right is that once Mrs L has paid back the capital balance of what's outstanding, the adverse information is then removed. However, I will require Tesco to adjust the reported monthly balances to reflect the refunds.

My final decision

For the reasons set out above, I uphold Mrs L's complaint.

I require Tesco Personal Finance PLC to:

- refund all interest, fees and charges from when the loan was first drawn; and
- pay 8% interest† on any overpayment from the date of payment until the date of settlement, if the effect of refunding all interest, fees and charges results in a credit balance being owed to Mrs L; and
- amend Mrs L's credit file to reflect the new monthly balances after refund of interest, fees and charges; and
- remove any related adverse information from Mrs L's credit file once the outstanding balance has been repaid; and
- arrange themselves, or through the debt collections agency, to agree an affordable and sustainable repayment plan for any remaining amount owed.

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

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs L to accept or reject my decision before 14 July 2022.

Dave Morgan
Ombudsman