DRN-3373874

The complaint

S, a limited company, complains about the way Funding Circle Ltd has administered lending arrangements. S is represented by a director, Mr P. For ease of reading, any reference to submissions or actions taken by Mr P refer to those taken on behalf of S.

What happened

Funding Circle provides a peer-to-peer lending platform and administers loans on behalf of both corporate and individual investors, who are the lenders in these arrangements. S held two loans administered by Funding Circle – one taken out in May 2017 (which I'll call "Loan A") and a second loan taken in October that year ("Loan B").

Mr P says that over the course of the loans S had various minor complaints with Funding Circle, but that what prompted this complaint was the difficult financial position that S found itself in during early 2020, during the Covid-19 pandemic. Due to the impact on S's business, Mr P made enquiries about reworking the loans or other forbearance that Funding Circle was able to offer. He says his broker was told that Funding Circle wouldn't consolidate the existing loans and that Funding Circle told him directly that it was unwilling to offer a payment holiday or any other assistance.

Mr P didn't want the accounts to default so he raised funds elsewhere. He attempted to pay off the loan balances, but had difficulty doing so. Mr P disputed the settlement figures Funding Circle provided, which appeared not to include any interest rebate for early repayment. Further, when Mr P paid the amount he believed was owed, Funding Circle first returned the money, and later – after it was resent – used the funds to pay off Loan B rather than Loan A. This left S with the higher £570 monthly payment of Loan A rather than the £279 that was payable under Loan B. Funding Circle used the balance of the overpayment towards the monthly payments due under Loan A.

In response to Mr P's concerns, Funding Circle said that during the pandemic it temporarily stopped arranging new commercial lending. It offered S a short-term payment plan for three months without adverse impact on S's credit file, although by that point Mr P had already made alternative arrangements. Funding Circle said that the settlement figures it provided to S included some accrued interest, which might account for the difference in Mr P's calculations. It also said that it had returned Mr P's lump sum payments as they were insufficient to clear the balances of both loans.

Mr P considers Funding Circle to have engaged in sharp practice, and that its actions caused unnecessary difficulty to S in operating its business. Although Mr P's correspondence references his other minor complaints, it is this issue that forms the core of his current dissatisfaction with Funding Circle and that is the subject of this decision.

Our investigator noted that the way in which Loan B was set up, with both the borrower and the lender being corporate bodies, took it outside the scope of our service. However, he was satisfied that this wasn't the case with Loan A, on which the lender comprised individual rather than corporate investors.

The investigator could find no record relating to Funding Circle's conversation with Mr P's broker, but noted Funding Circle had given the correct information to Mr P about loan consolidation. He said Funding Circle had told us that it was awaiting government guidance about Covid-19 forbearance measures, though this situation was in any event overtaken by Mr P being able to make alternative borrowing arrangements via friends and family.

In relation to the discrepancy between the settlement figures Funding Circle gave Mr P and those Mr P calculated for himself, the investigator concluded that Funding Circle had calculated the sums due in line with the respective loan agreements. But he thought Funding Circle should have done more to establish which loan was to be settled. Although Mr P had used the reference for Loan B when he resent his lump sum payment following its earlier return, the investigator felt Mr P's earlier correspondence made clear that he wanted to settle both loans, and why he was looking to do so. In light of this, the investigator thought Funding Circle should have obtained confirmation from Mr P rather than just applying his payment to Loan B.

To settle matters, the investigator recommended that Funding Circle rework the loan settlement arrangements to reflect Mr P's intention to settle Loan A in May 2020, including allowing Mr P to pay off any resultant shortfall on Loan B based on the settlement figure at that time. The investigator said that if that resulted in S having overpaid Loan B (due to payments subsequently received), Funding Circle should return these with interest. It should also remove any adverse payment information that it might have recorded.

Funding Circle didn't accept the investigator's recommendation. It provided further details of its correspondence with Mr P, which it considers support its position that it didn't act incorrectly in applying the payments as it did. Funding Circle sought to make the following points:

- Its business model meant it was unable to implement the investigator's recommendations. It had paid the Loan B investors when that loan was settled, and couldn't now recoup that money to use it towards Loan A. In addition to the technical difficulties that would cause, it would be unfair on the investors in both loans
- It disagreed with the investigator's statement that it would have been prudent for it to check which loan Mr P had intended to settle when he paid the lump sum a second time. It had used the lump sum payment to settle Loan B because that was the reference Mr P had used in sending the payment. It could not reach out to every customer making a payment to settle their loan to check whether they used the correct reference. Nor did it agree that it was certain S would have asked for the larger loan to be settled had it done so

Funding Circle acknowledged the financial strain S was under. It said if S couldn't maintain the loan payments it would need to record the account as being in default, but would then be able to restructure a more affordable repayment plan. It added that it was willing to pay £250 compensation in recognition of delays in dealing with S.

The investigator wasn't persuaded that Funding Circle had dealt with matters fairly, so the dispute has been passed to me for review and determination.

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.

As the investigator noted, the activity in which Funding Circle was engaged in respect of Loan B doesn't meet the definition of an Article 36H credit-related regulated activity, due to the corporate nature of both the borrower and lender in that situation. Nevertheless, I'm satisfied that this doesn't prevent me from considering the way in which Funding Circle administered the settlement payment. That's because doing so requires I take into account the position on Loan A, where the lender was made up of individual investors rather than a body corporate.

Calculation of the loan settlement figures

Both Loan A and Loan B operated on a fairly standard amortisation schedule with a fixed monthly payment. In broad terms, this means that in the earlier stages of the loan, a greater proportion of the monthly payment comprises interest than in the later stages, as interest is calculated on the prevailing balance. As the loan progresses, the proportion of the payment that goes towards capital repayment increases as the interest proportion reduces.

The loan agreements both provide for early settlement; that is, where the borrower wants to repay the balance before the end of the agreed loan term. They say that in this event, depending on the repayment date the amount required to settle may include additional interest of up to one month.

When Mr P sought to settle S's loans in 2020, Loan A had been running for nearly three years of a five-year term. On an unamortised schedule, that would mean capital payments of £5,500 each year, giving a settlement figure in the region of £10,500-£11,000 after three years. But on an amortised schedule, the settlement figure would be around £12,500. That sum is consistent with the amount Funding Circle told Mr P on 20 May 2020.

Similarly, Funding Circle's settlement figure of £6,620 looks to me to be broadly in line with the amortisation schedule for a five-year loan being settled around the halfway point, as was the case with Loan B. While I appreciate Mr P and his accountant reached markedly different figures using their own calculations, I'm satisfied Funding Circle gave the correct information when asked to provide settlement figures for S's loans.

Application of the settlement payments

Bearing this in mind, it's clear that the two payments Mr P sent Funding Circle on 13 May 2020 to settle the loans - £10,700 and £4,680 – were insufficient to achieve this. The loan agreements don't appear to make provision for part-payment of capital lump sums. So I can understand why Funding Circle returned Mr P's payments – the monies sent weren't the sums needed for settlement, and there was clearly disagreement between the parties over the amounts required to settle.

What's less clear is why Funding Circle took a different approach when Mr P resubmitted his payments on 29 May. The mere fact that Mr P gave the reference for Loan B on both payments is in my view insufficient for Funding Circle to have taken the approach it did. If anything, this should have indicated to Funding Circle that the information was incorrect; it suggested Mr P wanted to pay some £14,500 to settle a loan he'd recently been told required only £6,620 to settle. This, coupled with the fact Mr P structured the two payments on 29 May in the way he did, and the ongoing email exchanges between the parties regarding the dispute over the correct settlement figures doesn't suggest that it was appropriate for Funding Circle to apply the payments in the way it did. Rather, it should have sought to clarify Mr P's intentions and if necessary, return the money.

Noting Funding Circle's response to the investigator on this point, I should be clear that I don't expect a business to undertake such steps on every payment it receives. Nor do I believe that is what the investigator suggested. But where – as here – there is clear and ongoing evidence of a dispute and an obvious error, I take the view that it would be remiss for it not to do so.

Had Funding Circle taken these steps, it seems likely that Mr P would have remained in dispute over the settlement figures – at least, until such time as Funding Circle gave him a suitable explanation for the way in which it calculated the amounts in question. It appears to have been able to do so fairly quickly. Funding Circle's email of 5 June provides this explanation. Mr P would then have been able to consider which of the two loans he wanted to settle.

Given his stated purpose in doing so was to improve S's cashflow, I'm satisfied it's more likely than not that Mr P would have used the money to settle Loan A, on which the monthly payment was more than double that of Loan B. Mr P himself made this clear in his email (also 5 June 2020), as well as in his subsequent correspondence. Taking all of this into account, I respectfully disagree with Funding Circle's comment that it is by no means certain S would have wanted to settle the larger loan. That is precisely what the available evidence says S would have done.

Having carefully considered matters, I'm not persuaded Funding Circle treated S fairly in the way it dealt with the settlement payments. As a result, S had greater cashflow problems than it might otherwise have experienced if Funding Circle had dealt with things more appropriately. So I've gone on to consider how Funding Circle should put that right.

Putting things right

I understand the difficulty Funding Circle has cited in simply reversing what happened, reinstating Loans A and B and then applying the payments in the way S wanted. The way in which Funding Circle operates means that this wouldn't be a practical solution if it involved the original investors.

However, I don't believe it's necessary to do that in order to achieve the same result. The error was Funding Circle's, rather than that of its investors. Funding Circle doesn't need to recreate the original loan arrangements in order to put right any loss S has suffered as a result. It can instead calculate what the difference in cost would have been had the loan payments been applied as I'm satisfied S would have instructed if Funding Circle had given it the opportunity. That would produce a sufficiently similar end result, without the inherent difficulty Funding Circle has cited.

In terms of reworking, then, Funding Circle should:

1. run a calculation of payments received on Loan A since 1 June 2020 based on S having paid the quoted settlement figure of £12,589.07 by 11 June 2020
2. run a calculation of Loan B as if that loan hadn't been settled on 1 June 2020 and had instead continued to operate in line with the original agreement
3. apply the sum in 1. (being the amount S has overpaid on Loan A) to the calculation in 2., backdated to the date each payment was received
4. If, as I anticipate, these calculations show that S has overpaid Loan B, then any such overpayments should immediately be repaid to S, together with interest on each amount again backdated to the date each payment was received. This interest should be calculated at an annual rate of 8% simple
5. Any late or adverse payment information that may have been recorded by Funding Circle in relation to either loan should be removed

I have considered the possibility that S might have paid off both loans in 2020 if Funding Circle had taken suitable steps at the time to deal with the settlement payments. S has indicated it was able to secure borrowing, and it's possible S might have been able to use this to cover the shortfall (in the region of £4,400). However, there is insufficient evidence to enable me to say that it's more likely than not that it would have done so.

In its response to the investigator, Funding Circle has noted that there were occasions on which its handling of matters was delayed. Although this wasn't something the investigator picked up on, I must acknowledge the fact that Funding Circle has itself done so. Where a business has caused unnecessary material delay or inconvenience to a customer, I would expect it to offer an apology in the form of compensation, and I'm pleased to see that Funding Circle has proposed doing so here. I think the amount it has proposed is fair in the circumstances.

other matters

In closing, I note that Mr P has mentioned that he is also unhappy about agents' fees and commission he believes were added to the overall cost of the loans without disclosure. As the investigator explained, that was not an aspect raised with Funding Circle previously, and as such it's not for me to reach a finding on that matter in the context of this complaint. While he is of course at liberty to raise this as a separate matter with Funding Circle, noting that Mr P has copies of the loan documents that I have also seen, he might want to take further independent advice before doing so.

My final decision

For the reasons I've set out here, my final decision is that I uphold this complaint. To settle it, I require Funding Circle Ltd within 28 days of receiving Mr P's acceptance of this decision to take the following steps:

1. run a calculation of payments received on Loan A since 1 June 2020 based on S having paid the quoted settlement figure of £12,589.07 by 11 June 2020
2. run a calculation of Loan B as if that loan hadn't been settled on 1 June 2020 and had instead continued to operate in line with the original agreement
3. apply the sum in 1. (being the amount S has overpaid on Loan A) to the calculation in 2., backdated to the date each payment was received
4. If, as I anticipate, these calculations show that S has overpaid Loan B, then any such overpayments should immediately be repaid to S, together with interest on each amount again backdated to the date each payment was received. This interest should be calculated at an annual rate of 8% simple
5. Any late or adverse payment information that may have been recorded by Funding Circle in relation to either loan should be removed
6. pay S £250 compensation in recognition of the inconvenience experienced due to delays it has acknowledged in its handling of matters

If Funding Circle deducts tax from the interest element of this award, it should confirm to S that it has done so and provide it with any relevant tax deduction certificate.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr P, on behalf of S, to accept or reject my decision before 12 July 2022.

Niall Taylor
Ombudsman