DRN-3462705

The complaint

Mrs W complains about a guarantor loan provided to her by UK Credit Limited, trading as UK Credit, ("UK Credit"), which she says was unaffordable. Mrs W's complaint has been brought to this Service on her behalf by a claims' management company. But for ease, I shall refer below to all actions being taken by Mrs W.

What happened

UK Credit entered into an agreement for a guarantor loan for Mrs W on 21 March 2016. The loan was for £7,500 and was repayable by 60 monthly payments of £254.76. The interest rate was 32.6%, (37.9% APR). If Mrs W made each repayment when it was due, the total amount payable was £15,285.60. Part of the loan was to be used to repay a previous loan for £7,500 which Mrs W had taken out with UK Credit in September 2013. So, UK Credit used £5,372.81 from the loan proceeds to repay the 2013 loan and Mrs W received £2,127.19 from the 2016 loan. According to the most recent information I've seen (February 2022), the loan hasn't yet been repaid.

Mrs W says that UK Credit didn't properly undertake affordability checks when granting her credit nor did it assess signs of her over indebtedness. She said that the unaffordable high cost loan worsened her financial situation which was already poor.

In its final response letter, UK Credit said an affordability assessment was conducted with Mrs W prior to the completion of the loan. This involved a review of information provided by its credit checks, an electronic income verification check, and a review of Mrs W's income and expenditure. Its credit checks showed that in general Mrs W was managing her financial commitments well . She already had an existing loan with it and had made all contractual monthly repayments. Following its income and expenditure assessment, UK Credit estimated that Mrs W had a surplus income of approximately £271 per month, and the loan was deemed affordable.

Our investigator's view

Our investigator recommended that Mrs W's complaint should be upheld. She didn't think that UK Credit's checks had gone far enough. She noted that Mrs W's total repayments towards other credit were already over £1,000, and with this loan, it would mean her total debt to income ratio would be around 75%. She said that this wouldn't be sustainable for the term of the loan, and as UK Credit was aware of this, she thought that UK Credit didn't make a fair lending decision. The investigator said that Mrs W had provided this Service with her bank statements prior to the approval of this loan. She noted that Mrs W was making payments to nine different accounts which were all with a debt collection agency and that Mrs W was constantly living in her £2,000 overdraft.

UK Credit responded to the investigator's view by asking to see the bank statements the investigator had referred to in her view. UK Credit reviewed the statements and disagreed with the investigator's view. It said:-

- Mrs W's active credit was under £12,000 which didn't seem disproportionate to her

income. Her existing loan repayments were £389.04 (without its 2013 loan). It queried how the investigator had calculated Mrs W's other credit to be over £1,000.
- Mrs W had maintained her loan repayments on its existing loan, and she was in an arrangement to pay her default balances.
- The investigator referred to a recent default for £30 but it noted that this account had been showing signs of payment difficulty 18 months previously, around the same time as other defaults had occurred. It seemed unrealistic to conclude that Mrs W was experiencing financial difficulty at the time of the loan application on this basis.
- Although nine defaults were with a debt collector, the default balances were reducing. It could see no evidence on the bank statements that payments to these items of credit were putting Mrs W into financial difficulty.
- It had seen a payslip to evidence Mrs W's monthly income as £1,775.74.
- Although Mrs W paid a monthly fee of £27 for her overdraft facility, and she went a few pounds over the overdraft just after Christmas 2016, she maintained her finances within this facility.
- From its assessment at the time, it didn't appear that the payday loan repayment of £300 had been taken into account.
- In terms of affordability, it didn't take the monthly payments totalling £400 from Mrs W's adult children into account. Mrs W had said she used this for non-essential spending. It felt that it was reasonable to take this into account for the purposes of considering whether she could afford the loan repayments with all her household income.
- There were regular payments going into Mrs W's current account from another account. There were also no regular payments to a payday lender appearing on Mrs W's bank statements.
- If UK Credit had seen Mrs W's bank statements at point of sale, it didn't believe there was sufficient evidence to suggest this loan was unaffordable.

As this complaint hadn't been resolved informally, it was passed to me, as an ombudsman, to review and resolve.

my provisional decision

After considering all the evidence, I issued a provisional decision on this complaint to Mrs W and to UK Credit on 7 April 2022. I summarise my findings:

I'd said that where information was conflicting or incomplete, I needed to make my decision on the balance of probabilities, which was what I'd done in relation to certain aspects of the complaint.

I'd noted that when UK Credit lent to Mrs W, the regulator was the Financial Conduct Authority ("FCA") and relevant regulations and guidance included its Consumer Credit Sourcebook ("CONC"). Its rules and guidance obliged UK Credit to lend responsibly. As set out in CONC, this meant that UK Credit needed to take reasonable and proportionate steps to assess whether or not a borrower could afford to meet its loan repayments in a sustainable manner over the lifetime of the loan agreement.

Repaying debt in a sustainable manner meant being able to meet repayments out of normal income while meeting normal outgoings and not having to borrow further to meet those repayments.

The lender was required to carry out a borrower focussed assessment each time - sometimes referred to as an "affordability assessment" or "affordability check". Neither the law nor the FCA specified what level of detail was needed to carry out an appropriate assessment or how such an assessment was to be carried out in practice. The FCA said that the level of detail would depend on the type of product, the amount of credit being considered, the associated cost and risk to the borrower relative to the borrower's financial situation, amongst other factors.

The checks had to be "borrower" focussed – so UK Credit had to think about whether Mrs W could sustainably repay her loan. In practice, this meant that the lender had to ensure that making the payments to the loan wouldn't cause Mrs W undue difficulty or adverse consequences. 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 loan repayments on Mrs W.

In general, I'd have expected a lender to require more assurance the greater the potential risk to the borrower of not being able to repay the credit in a sustainable way. So, for example, I'd have expected a lender to seek more assurance, potentially by carrying out more detailed checks

- the lower a person'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 was likely to be greater and the borrower would be required to make payments for an extended period);

I'd noted that UK Credit had spoken to Mrs W on the phone and gathered some information from her about her income and expenses before it agreed the loan. Mrs W had provided UK Credit with a payslip for February 2016. It had also carried out a credit check.

Mrs W's payslip for February 2016 showed a net monthly pay of £1,775.74. But it also showed an amount of £63.60 for expenses included in the payment. So, her net monthly income was around £1,712 without expenses which was a little less than the amount of £1,726.01 used by UK Credit in its affordability calculations.

I'd listened to a recording of the call between UK Credit and Mrs W in which Mrs W had provided the lender with more information about her employment, outgoings, and credit commitments. I'd also noted that she'd said that her two adult children were paying her a total of £400 each month. In its final response letter, UK Credit said that it didn't take this additional income into account for the purposes of the affordability assessment and relied solely on Mrs W's employment income. But I'd noted in its response to the investigator's view that it felt it was reasonable to take this extra income into account for the purposes of considering whether Mrs W could afford the loan repayments with all her household income. I didn't think it was reasonable to take this additional income into account. UK Credit was required to assess whether Mrs W could afford to meet its loan repayments in a sustainable manner over the lifetime of the agreement. As the loan was for 60 months, I didn't think Mrs W could reasonably expect her two adult children to live with her and contribute a payment for board for the whole of that period.

I'd also reviewed UK Credit's credit checks. These showed Mrs W had eight defaulted accounts between 2010 and 2014. Generally, I thought it would be more reasonable for a lender to be more interested in a consumer's more recent credit history for the purposes of assessing whether a loan would be affordable. I could also see that Mrs W was paying off some of the defaults through a debt collection agency. UK Credit in its final response letter appeared to have allocated around £50 for these payments. But I'd also noted that an older account for just £30 which had been in arrears for at least 23 months, had been defaulted in the same month as Mrs W's loan application. I thought it was concerning that Mrs W had been unable to settle this debt before it was defaulted. And I didn't think the proximity of the default to the loan application made it responsible for UK Credit to provide the loan without more comprehensive checks.

The checks also showed that Mrs W had two loans, although one of these was UK Credit's 2013 loan. The other loan was for £4,000 and had been taken out around four months prior to the loan application. I understood that this was a high cost loan with monthly repayments of £195. I could see that Mrs W had also taken out two retail option loans totalling over £3,200 around nine months earlier with monthly repayments totalling around £141. I could also see that Mrs W's current account had a £2,000 overdraft limit and her overdraft balance was £1,963. So, she was approaching her overdraft limit. There was also an account with a communications supplier with a balance of £258 on which it appeared that Mrs W had missed four of the last five payments. I could also see a payday loan which was taken out in 2012 which had been in arrears for at least 14 months. I couldn't see that any payday loans had been taken out since 2012. Altogether, I thought UK Credit ought to have been concerned about Mrs W's relatively recent large increase in credit, the recent arrears on a communications account and her current account approaching its overdraft limit, all of which might have suggested that Mrs W's finances were under pressure. I thought Mrs W's recent use of credit, should have led UK Credit to conclude it should gather some more information about Mrs W's finances.

I was also concerned that UK Credit appeared to have mostly relied on Mrs W's statement of her expenses without verifying them. CONC 5.3.1(4) said:

If a firm takes income or expenditure into account in its creditworthiness assessment required under CONC 5.2.2R (1):

(a) The firm should take account of actual current income or expenditure and reasonably expected future income or expenditure (to the extent it is proportionate to do so) where it is reasonably foreseeable that it would differ from actual current income or expenditure over the anticipated repayment period of the agreement;

(b) it is not generally sufficient for a firm to rely solely for its assessment of the customer's income and expenditure, on a statement of those matters made by the customer;

So, in Mrs W's circumstances, I didn't think it was reasonable for UK Credit to base its assessment on the financial information Mrs W had provided about her expenses. Mrs W was entering into a significant commitment with UK Credit. She would need to make monthly repayments of around £255 for 60 months. So, I would have expected that UK Credit would want to gather, and independently check, some detailed information about Mrs W's financial circumstances before it agreed to lend to her. I didn't think that UK Credit's checks went far enough. I thought it would have been proportionate for UK Credit to have independently checked the true state of Mrs W's finances before agreeing the loan.

UK Credit was required to establish whether Mrs W could make her loan repayments without experiencing adverse consequences and not just to ascertain whether the loan repayments were technically affordable on a strict pounds and pence calculation.

But although I thought UK Credit should have asked for some additional information before agreeing the loan, that in itself didn't mean that Mrs W's complaint should succeed. I also needed to be persuaded that any further information would have shown UK Credit that

Mrs W couldn't sustainably afford the repayments. So, I'd looked at Mrs W's bank statements, to see what additional checks would have shown the lender.

I wasn't suggesting that this was the exact check that UK Credit should have carried out. But I did think UK Credit needed information to corroborate what Mrs W said was happening with her finances. And looking at her bank statements was one way of achieving that although there were of course many other ways that level of detail could have been established. But I thought that by looking at Mrs W's bank statements I could get a good idea of what further checks might have shown.

What would further checks have shown?

I'd noted that Mrs W had sent this Service some statements for two of her current accounts for parts of several months. It was clear from the statements that she was making transfers to her accounts from four other accounts. So, I'd asked the investigator to ask Mrs W for bank statements for a complete month's period for all of her accounts and for some more information about her situation to see what better checks would have shown UK Credit.

Mrs W said she was unable to provide bank statements for one of her current accounts and she could only provide statements for part of a period for another. She'd provided statements for two accounts that were only used for transfers between accounts. She'd also said that she paid for gas and electricity and sometimes her council tax by cash. So, I'd used the amounts Mrs W provided on the phone to UK Credit for the amounts paid for her utilities and council tax.

I'd reviewed all the bank statements we'd received from Mrs W to give me the best picture of what the lender should have seen if it had made better checks.

With regard to the account into which Mrs W's salary was paid, I could see that there was an overdraft limit of £2,000 and that Mrs W generally stayed within the overdraft limit. But she only did this by transferring amounts from her other accounts into her main account. And at the date of her loan application, her overdraft was nearly £1,999 and so it was just under the overdraft limit. So, it appeared that Mrs W's finances were likely to be strained.

I'd reviewed Mrs W's bank statements from three of her current accounts for the period 10 February 2016 to 7 March 2016 which was almost a complete month. I could see there were transfers totalling around £818 into the accounts with transfers of around £164 paid out of the accounts. During this period, I could see that Mrs W was paying in total from three of her current accounts around £1,635 for her rent, regular living costs (including cash payments for utilities and council tax) and credit commitments (excluding the loan repayment for her 2013 UK Credit loan). This wouldn't have left Mrs W with sufficient disposable income to repay UK Credit's 2016 loan. I'd also looked at Mrs W's bank statements for a period of around a month from mid-December 2015 to mid-January 2016 which produced a similar result. Overall, I could see from the bank statements that Mrs W's financial commitments and regular living costs were higher than the amount UK Credit had calculated. And I couldn't see that Mrs W had sufficient disposable income to repay UK Credit sustainably.

So, I thought if UK Credit had carried out what I considered to be proportionate checks, it was likely it would have discovered that Mrs W was over committed financially. And I thought it was likely that further checks wouldn't have provided any reassurance to UK Credit that Mrs W would have managed her repayments sustainably or that the loan was suitable for her. And so, I thought the lender was irresponsible to have agreed to lend to her on this occasion.

So, for the reasons set out above, I intended to say that UK Credit didn't make a fair lending decision when it provided the loan to Mrs W and subject to any further representations by Mrs W or UK Credit, I intended to uphold Mrs W's complaint and say that UK Credit should put things right as follows.

Putting things right – what UK Credit needs to do

I understand that the loan hasn't been fully repaid. In order to put Mrs W back into the position she would have been had the loan not been agreed for her, UK Credit needs to ensure that Mrs W only repays the principal borrowed on the loan. In other words, Mrs W shouldn't repay more than the capital amount of £7,500 she borrowed. So, UK Credit needs to:

a) treat all payments that Mrs W has made towards the loan as payments towards the principal amount borrowed;
b) if Mrs W has made payments above the capital amount of £7,500, then these should be refunded to her, along with simple interest at the rate of 8% per year on these amounts from the date they were paid to the date of settlement*;
c) if Mrs W hasn't made payments above the capital amount of £7,500 and there is still an outstanding capital balance then UK Credit needs to treat Mrs W fairly and sympathetically in this matter. This may mean agreeing a mutually agreeable repayment plan with her; and
d) remove any adverse information about the loan from Mrs W's credit file.

If UK Credit has sold the outstanding debt on the loan, it should buy it back if it is able to do so or chooses to do so and then take the steps listed above. If UK Credit isn't able to buy the debt back or chooses not to, then it should liaise with the new debt owner to bring about steps a) to d) above.

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

Mrs W responded to my provisional decision to say that she was happy with it.

UK Credit disagreed with my provisional decision and raised a number of issues. I list below UK Credit's main points:-

- It didn't dispute that the employed income to be taken into account should be the lowest pay. It agreed that Mrs W's employed income was £1,712 as detailed in the decision.

- It didn't agree with my conclusion that the additional income Mrs W received in board payments from her adult children should be excluded. It noted that Mrs W had said that the board payments were used for non-essential spending. It felt it was reasonable to take this into account for the purposes of considering whether Mrs W could afford the loan repayments with all her household income. It also noted that Mrs W's circumstances were expected to change with her impending wedding and her partner was then expected to share the household costs when moving into her residence. It said that not only was Mrs W in receipt of board from her two adult children, and she didn't allude to this changing during the loan term, but also she specifically told its agent that she would also be expecting to share the household expenditure after her wedding in or around five months' time, thereby decreasing her contribution to the household bills.

- Regarding what was seen on the bank statements, it noted that only one month was taken into consideration and not all account statements were provided. It noted on the bank statements that Mrs W had a total of six bank accounts, but it had only seen statements for two of the accounts. On the basis it hadn't seen all of the accounts, it was unsure that there was sufficient evidence to draw conclusions on the affordability of its loan repayments.

- It said that based on Mrs W's income of £1,711, and not including the contributions from her adult children and the future contributions from Mrs W's husband to be, the loan should still have been affordable based on the essential spending on Mrs W's bank statements and what she had told its agent at the point of sale. It listed the following expenses:-

Council tax	£113
Electric	£80
Gas	£50
Water	£23
Media	£127.34
Mobile	£20
TV licence	£12.10
Rent	£335
Food	£100
Overdraft fee	£27
Default debts	£90
Retail credit	£141
Loan repayment	£195
UKC loan	£254.76
Credit check	£3.99
Total expenses	£1,572.19
Surplus income	£138.81

- After the loan was paid out, Mrs W maintained her monthly direct debit repayments. She had changed jobs on more than one occasion during the loan term which did affect her repayments in May 2017. Looking at the credit search it ran in 2021 as part of its investigation, Mrs W only started to show signs of being in financial difficulty after she took out more credit from March 2017, some 12 months after its loan commenced.

- Based on the evidence available at point of sale and the bank statements that it had received from this Service, it didn't agree that Mrs W was over committed financially and that its loan repayments were unsustainable.

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.

I have also taken into account the law, any relevant regulatory rules and good industry practice at the time.

I have considered carefully UK Credit's response to my provisional findings. I appreciate that this will be very disappointing for it, but I am still of the view that it didn't make a fair lending decision when it agreed the loan for Mrs W. I've explained my reasons in my provisional decision and I've also responded to its main points in response to my provisional decision below.

I note that UK Credit agreed that a monthly income of £1,712 should be used, although later in its response it used a monthly income of £1,711 in its affordability calculations.

I refer to the board payments from Mrs W's adult children which UK Credit felt should be taken into account. I think it might be reasonable in certain situations to include such payments as part of a consumer's income depending on the circumstances, such as the term of the loan and the degree to which the repayments relied on a contribution from others. In this case it seems the loan wasn't affordable sustainably without such a contribution. But as the loan term was five years it seems unreasonable to assume that Mrs W could depend on others for her repayments across the entire term.

I'd also asked the investigator to ask Mrs W if she expected her adult children to continue to live with her after her wedding. Mrs W responded to say that at the time of the loan application, she didn't really expect her adult children to continue living with her after the wedding. And one of her children had been looking to rent somewhere to live. Mrs W also said that the board payments weren't regular and one of her children wouldn't pay anything for months because they were in and out of jobs.

So, in the circumstances of this case, I don't think it was appropriate for UK Credit to take the board payments into account.

I refer to UK Credit's comments with regard to the expected change in Mrs W's circumstances as a result of her impending wedding and her partner then being expected to share the household costs when moving into her residence. I don't think it was appropriate to take this into account. At the time of the loan application, it doesn't appear that UK Credit had any information as to Mrs W's new partner's circumstances, the amount he would contribute, and it didn't know what his situation would be after the wedding which was around five months' after the loan was provided. It was also important that Mrs W could afford the loan until the wedding from her own income.

I note that CONC 5.2.3G(4) said the extent and scope of the creditworthiness assessment should be dependent upon and proportionate to factors which might include the financial position of the customer at the time of seeking the credit.

And CONC 5.3.1G(3) said:-

"A firm in making its creditworthiness assessment or the assessment required by CONC 5.2.2R (1) may take into account future increases in income or future decreases in expenditure, where there is appropriate evidence of the change and the repayments are expected to be sustainable in the light of the change."

In this case as I've said above, I don't think Mrs W could afford the loan sustainably at the time she sought credit from UK Credit and there was a gap of at least five months before she was to be married. I've also not received and seen appropriate evidence of the change in circumstances. So, I don't think it was right for UK Credit to accept Mrs W's application on this basis.

I also note that UK Credit didn't think there was sufficient evidence to draw conclusions on the affordability of its loan repayments. I disagree. As well as the statements I'd seen for the period 10 February 2016 to 7 March 2016, as I'd said above I'd also reviewed some statements for the period of around a month from mid-December 2015 to mid-January 2016 which supported my findings regarding the affordability of the loan repayments. I had also seen statements for three other accounts, and two of the accounts were only used for transfers. With regard to the statements for the account I hadn't seen, Mrs W said the account wasn't used for any real purpose.

I've recalculated Mrs W's likely living costs and compared them to the list provided by UK Credit in its response to my provisional decision. I disagree with some of the figures provided by UK Credit where they differ from the information in Mrs W's bank statements for the period 10 February 2016 to 7 March 2016. I note that UK Credit said it had used the information provided by Mrs W in its call with her and the bank statements it had received from this Service. As I'd said above, I don't think UK Credit should have relied on Mrs W's statement of her expenses without verifying them. But it seems to have mainly listed the figures Mrs W provided to its agent.

Other than the amount of £266 for utilities and council tax which Mrs W said were paid by cash, I'd used all but one of the figures in my calculation of Mrs W's expenses from the bank statements for two of Mrs W's bank accounts which this Service had previously sent to UK Credit. There was also an amount of £5 likely to be for food on another account statement UK Credit hadn't seen. On balance, it appeared that spending on food and drink totalled around £360 (rather than the amount of £100 listed by UK Credit), spending on a TV Licence was £29.10 (and not £12.10 as listed by UK Credit), and rent was £339.78 (and not £335 as listed by UK Credit). The figures I'd used to calculate Mrs W's credit repayments to two of her other creditors were also slightly higher than those used by UK Credit.

I'd calculated Mrs W's living costs and financial commitments on this occasion to be around £1,577 (excluding UK Credit's loan repayment). This left a monthly disposable income of around £135 which wasn't sufficient to meet UK Credit's loan repayment of £254.76. So, I didn't agree with UK Credit that the loan was affordable for Mrs W.

I note that UK Credit said that after the loan was paid out, Mrs W maintained her monthly direct debit repayments. It also said she had changed jobs which did affect her repayments in May 2017. But I can see from UK Credit's loan account statement that Mrs W had earlier payment difficulties. Her repayment was late in August 2016 and her direct debit was returned in January 2017 after which she made a late repayment.

So, for the reasons set out above, I see no reason to alter my provisional conclusions. It follows that I uphold this complaint and require UK Credit to take the steps set out above under the heading "Putting things right – what UK Credit needs to do".

My final decision

My decision is that I uphold this complaint. In full and final settlement of this complaint, I order UK Credit Limited, trading as UK Credit, to take the steps set out above under the heading "Putting things right – what UK Credit needs to do".

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs W to accept or reject my decision before 19 July 2022.
Roslyn Rawson
Ombudsman