

Complaint

Mrs S has complained that Tesco Personal Finance PLC (trading as “Tesco Bank”) provided her with an unaffordable loan. She says that she was already £30,000.00 in debt at the time of the application and proportionate checks would have shown this as well as the fact that she shouldn't have been lent to.

Background

Tesco Bank initially provided Mrs S with a loan for £5,000.00 in February 2017. The loan had an APR of 3.8% and a 48-month term. This meant that the total amount to repay of £5,390.40, which included interest of £390.40 was due to be repaid in 48 monthly instalments of just over £112. Mrs S in fact settled this loan in full a few months after.

Tesco Bank subsequently provided Mrs S with a loan for £20,000.00 in May 2018. The loan had an APR of 5.3% and a 120-month term. This meant that the total amount to repay of £25,882.80, which included interest of £5,882.80 was due to be repaid in 120 monthly instalments of just over £215.

One of our investigators looked at this complaint and thought that Tesco Bank didn't act unfairly or unreasonably when providing loan 1. But he also thought that Tesco Bank shouldn't have provided loan 2 as reasonably and proportionate checks would have shown it that the loan was unaffordable for Mrs S. Mrs S didn't disagree with our investigator's assessment. But Tesco Bank did disagree and asked for an ombudsman to review the complaint.

As the parties appear to be in agreement over the position relating to loan 1, this decision is only looking at whether Tesco Bank acted fairly and reasonably when providing Mrs S with loan 2. And all reference made to loan from this point is made with reference to loan 2 which was provided in May 2018.

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.

We've set out our general approach to complaints about unaffordable/irresponsible lending - including the key rules, guidance and good industry practice - on our website. And I've referred to this when deciding Mrs S' complaint.

Having carefully thought about everything, I think that there are two overarching questions that I need to answer in order to fairly and reasonably decide Mrs S' complaint. These two questions are:

1. Did Tesco Bank complete reasonable and proportionate checks to satisfy itself that Mrs S would be able to repay her loan without experiencing difficulty or suffering significant adverse consequences?

- o If so, did it make a fair lending decision?
- o If not, would those checks have shown that Mrs S would've been able to do so?

2. Did Tesco Bank act unfairly or unreasonably in some other way?

Did Tesco Bank complete reasonable and proportionate checks to satisfy itself that Mrs S would be able to repay her loan without experiencing difficulty or suffering significant adverse consequences?

Tesco Bank provided this loan while it was authorised and regulated by the Financial Conduct Authority ("FCA"). The rules and regulations in place required Tesco Bank to carry out a reasonable and proportionate assessment of Mrs S' ability to make the repayments under these agreements. This assessment is sometimes referred to as an "affordability assessment" or "affordability check".

The checks had to be "borrower" focused – so Tesco Bank had to think about whether repaying the loan would cause significant adverse consequences *for Mrs S*. In practice this meant that Tesco Bank had to ensure that making the payments to the loans wouldn't cause Mrs S undue difficulty or adverse consequences.

In other words, it wasn't enough for Tesco Bank to simply think about the likelihood of it getting its money back, it had to consider the impact of the loan repayments on Mrs S. Checks also had to be "proportionate" to the specific circumstances of the loan application.

In general, what constitutes a proportionate affordability check will be dependent upon a number of factors including – but not limited to – the particular circumstances of the consumer (e.g. their financial history, current situation and outlook, and any indications of vulnerability or financial difficulty) and the amount / type / cost of credit they are seeking. Even for the same customer, a proportionate check could look different for different applications.

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 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 is likely to be greater and the customer is required to make payments for an extended period); and
- the *greater* the number and frequency of loans, and the longer the period of time during which a customer has been given loans (reflecting the risk that repeated refinancing may signal that the borrowing had become, or was becoming, unsustainable).

There may also be other factors which could influence how detailed a proportionate check should've been for a given loan application – including (but not limited to) any indications of borrower vulnerability and any foreseeable changes in future circumstances.

I've carefully thought about all of the relevant factors in this case.

Were Tesco Bank's checks reasonable and proportionate?

Tesco Bank says it agreed to Mrs S's application after she provided details of her monthly income and some information on her expenditure. It says it cross-checked this against information on a credit search it carried out and all of this information showed Mrs S could comfortably make the repayments she was committing to. On the other hand, Mrs S has said she should never have been accepted for such a large loan on her income.

I've thought about what Tesco Bank has said. But I have concerns at some of the information relied upon. Firstly, Tesco Bank doesn't appear to have taken any steps to have checked Mrs S' income. Tesco Bank has said that Mrs S had an obligation to provide true and accurate information. I agree that prospective borrowers should provide full and accurate information. But I think that Tesco Bank is overlooking its own obligations here. CONC 5.3.1G(4) states:

(a) 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 I don't think that it's fair and reasonable for Tesco Bank to suggest it was misled by Mrs S' failure to provide true and accurate information, when it should have obtained enough information to have made an informed decision and it appears to have been selective in which CONC 5.2 obligations it chose to meet. This is especially as I don't know how its question regarding monthly income was even framed to Mrs S and Tesco Bank was advancing a significant sum over an extended term. In these circumstances, I consider Tesco Bank's use of inflammatory language such as 'application fraud' to be particularly unhelpful here.

Furthermore, I also think that the situation was exacerbated by the fact that Tesco Bank, at best, chose to use statistical data to validate Mrs S' declaration of her living expenses. I accept that there is a place for the use of statistical data in income and expenditure assessments. However, I don't think this is in circumstances where a borrower is being lent such a large amount over an extended period of time and without any validation of income.

Bearing in mind the particular circumstances of the borrowing here, I do think that Tesco Bank ought to have obtained further information before agreeing to provide this loan to Mrs S. As there's no evidence that Tesco Bank asked for, or considered, further information, I find that it didn't complete fair, reasonable and proportionate affordability checks before providing Mrs S with this loan.

Would reasonable and proportionate checks have indicated to Tesco Bank that Mrs S would have been unable to repay this loan?

As reasonable and proportionate checks weren't carried out before this loan was provided, I can't say for sure what they would've shown. So I need to decide whether it is more likely than not that a proportionate check would have told Tesco Bank that Mrs S would've been unable to sustainably repay this loan.

Mrs S has provided us with evidence of her financial circumstances at the time she applied for this loan. Of course, I accept different checks might show different things. And just because something shows up in the information Mrs S has provided, it doesn't mean it would've shown up in any checks Tesco Bank might've carried out. But in the absence of anything else from Tesco Bank showing what this information would have shown, I think it's

perfectly fair, reasonable and proportionate to place considerable weight on it as an indication of what Mrs S' financial circumstances were more likely than not to have been at the time.

I've seen the comments Tesco Bank regarding Mrs S having made her loan repayments (bar a temporary period where she made use of a temporary payment holiday) and this in itself being indicative of the loan being affordable. But I don't agree with Tesco Bank's argument here because it was required to establish whether Mrs S could sustainably make her loan repayments.

The regulator defined this as being without difficulty and without having to borrow further. And Mrs S simply having made her payments doesn't in itself demonstrate that she did this without difficulty or the need to borrow further. Indeed, I note that Tesco Bank itself has referred to the fact that Mrs S approached it for a further advance of £10,000.00 in May 2019. This application might have been declined but nonetheless it might be indicative of the fact that Mrs S was looking to borrow further to keep up with her existing commitments.

I've carefully considered the information Mrs S has provided. Having done so, it's clear that Mrs S was earning less than Tesco Bank believed her to be. And her most of her income was pretty much being used to meet her existing credit and living commitments. Furthermore, Mrs S' bank statements also show that she was regularly overdrawn too.

I've seen that Tesco Bank's response to our investigator quoted an extract from an ombudsman's decision regarding the use of an overdraft not in itself being an indication of financial difficulty. However, I'm not sure of the relevance of this extract here, given I'm not considering whether Tesco Bank should have continued providing Mrs S with an overdraft. What I'm considering here is whether Mrs S could make her payments to this loan without undue difficulty or borrowing further. The fact that Mrs S was entering her overdraft (and therefore borrowing) each month leads me to conclude that she was always likely to be relying on borrowing further in order to make her loan payments.

Bearing all of this in mind, I'm satisfied that reasonable and proportionate checks would more likely than not have demonstrated that Mrs S was unlikely to have been able to make the repayments to this loan without borrowing further and/or suffering undue difficulty. And, in these circumstances, I find that reasonable and proportionate checks would more likely than not have alerted Tesco Bank to the fact that Mrs S would not be able to sustainably make the repayments to this loan.

As this is the case and given what exactly it was Tesco Bank was required to consider, I'm satisfied that Tesco Bank's decision to provide this loan to Mrs S wasn't fair and reasonable in the circumstances.

Did Tesco Bank act unfairly or unreasonably towards Mrs S in some other way?

I've carefully thought about everything provided. And having done so, I've not seen anything to suggest that Tesco Bank acted unfairly or unreasonably towards Mrs S in some other way.

Did Mrs S lose out as a result of Tesco Bank unfairly providing him with his loan?

As Mrs S paid and she's still being expected to pay interest, fees and charges on a loan that she shouldn't have been provided with, I'm satisfied that she has lost out as a result of what Tesco Bank did wrong.

So I think that Tesco Bank needs to put things right.

Fair compensation – what Tesco Bank needs to do to put things right for Mrs S

Having thought about everything, Tesco Bank should put things right for Mrs S by:

- Removing all interest, fees and charges applied to Mrs S' loan from the outset. The payments Mrs S made should be deducted from the new starting balance – the £20,000.00 originally lent. Tesco Bank should treat any payments made should the new starting balance be cleared as overpayments. And any overpayments, if there are any, should be refunded to Mrs S;
- Adding interest at 8% per year simple on any overpayments, if any, from the date they were made by Mrs S to the date of settlement†;
- If an outstanding balance remains on Mrs S' loan once these adjustments have been made, Tesco Bank should contact Mrs S to arrange a suitable repayment plan for this.
- If, after all adjustments have been made, no outstanding balance remains, Tesco Bank should remove any and all adverse information it may have recorded about this loan from Mrs S' credit file.

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

My final decision

For the reasons I've explained, I'm upholding Mrs S' complaint. Tesco Personal Finance PLC needs to put things right in the way set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs S to accept or reject my decision before 29 July 2022.

Jeshen Narayanan
Ombudsman