DRN-3584017

Complaint

Mr S has complained that Zopa Bank Limited ("Zopa") provided him with an unaffordable loan.

Background

Zopa provided Mr S with a loan of £10,000.00 in June 2021. This loan had an APR of 28% and an 60-month term. This all meant the total amount repayable of £17,579.07, which included interest and charges of £7,579.07, was due to be repaid in 60 instalments of £292.98.

One of our investigators looked at this complaint and thought that Zopa unfairly provided this loan to Mr S as proportionate checks would have shown it was unaffordable. Zopa disagreed with our adjudicator and asked for an ombudsman to review the complaint.

My findings

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 Mr 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 Mr S' complaint. These two questions are:

1. Did Zopa complete reasonable and proportionate checks to satisfy itself that Mr S would be able to repay his loan in a sustainable way?

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

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

__Did Zopa complete reasonable and proportionate checks to satisfy itself that Mr S would be able to repay his loan in a sustainable way?__

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

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

In other words, it wasn't enough for Zopa to simply think about the likelihood of it getting its money back, it had to consider the impact of the loan repayments on Mr 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 Zopa's checks reasonable and proportionate?

Zopa says that it carried out an income and expenditure assessment with Mr S prior to providing him with this loan. It also carried out a credit check. Mr S declared that he was earning £40,000.00 a year. Zopa also determined that once Mr S' expenditure was deducted from his income he'd be left with just under £900 in disposable income each month. In its view this left Mr S with enough to be able to make the payments to this loan.

I've carefully considered what Zopa has said. But the credit check it carried out showed Mr S was significantly indebted. And on top of this Mr S was right at his credit limit on more than one of his revolving credit accounts. So the disposable income arrived at for Mr S didn't really tally with someone with his credit file.

Bearing in mind all of this, I think that Zopa ought to have carried out further checks in relation to Mr S' expenditure in order to address the mismatch between what the credit file was showing and the monthly disposable income amount arrived at, before it agreed to advance these funds. I say this while especially mindful that the purpose of this loan was recorded as other and therefore there's no suggestion that Mr S might have used the proceeds of this loan to consolidate his existing debts.

As I can't see that Zopa did take further steps to verify Mr S' expenditure, I don't think that the checks it carried out before providing Mr S with this loan were reasonable and proportionate.

Would reasonable and proportionate checks have indicated to Zopa that Mr 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 Zopa that Mr S would have been unable to sustainably repay this loan.

It's clear that a lot of the back and forth on this case has centred on whether Zopa knew or ought to have known that Mr S had taken out a £25,000.00 loan with another lender around 7 or so weeks before this one. I don't know if Zopa was aware of Mr S' £25,000.00, the records of its credit checks suggest, but I don't think that this doesn't matter too much anyway.

I say this because Zopa was required to establish whether Mr S could make his loan repayments without experiencing significant adverse consequences – not just whether the loan payments were technically affordable on a strict pounds and pence calculation. And I've carefully considered all of the information provided in light of this.

Having done so, it's clear to me that Mr S was struggling to manage his existing commitments, even without the £25,000.00 loan being included. Mr S never existed his overdraft and the information I've seen clearly shows why this is the case. So I think that proportionate checks would have shown Zopa that Mr S was likely to use this loan for unsustainable purposes and that he would more likely than not use borrowed funds to make the payments to this loan.

Bearing all of this in mind, I'm satisfied that reasonable and proportionate checks would more likely than not have demonstrated that Mr S would not 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 Zopa to the fact that Mr S was in no sort of position to make the payments on this loan without suffering significant adverse consequences.

Did Zopa act unfairly or unreasonably towards Mr S in some other way?

I've carefully thought about everything provided. And having done so, I've not seen anything to suggest that Zopa acted unfairly or unreasonably towards Mr S in some other way. So I don't think Zopa acted unfairly or unreasonably towards Mr S in some other way.

Did Mr S lose out as a result of Zopa unfairly providing him with this loan?

As Mr S has paid and is being expected to pay interest and charges on a loan that he shouldn't have been provided with, I'm satisfied that he has lost out as a result of what Zopa did wrong.

So I think that Zopa needs to put things right.

Fair compensation – what Zopa needs to do to put things right for Mr S

Having thought about everything, Zopa should put things right for Mr S by:

- removing all interest, fees and charges applied to the loan from the outset. The payments Mr S made, whether to Zopa or any other party, should be deducted from the new starting balance – the £10,000.00 originally lent. If Mr S has already repaid more than £10,000.00 then Zopa should treat any extra as overpayments. And any overpayments should be refunded to Mr S;

- adding interest at 8% per year simple on any overpayments, if any, from the date they were made by Mr S to the date of settlement†;

- if an outstanding balance remains after all adjustments have been made, Zopa should set up an affordable payment plan with Mr S. I would remind Zopa of its obligation to exercise forbearance and due consideration, in the event Mr S is experiencing financial difficulty, when arranging such a plan;

- if no outstanding balance remains after all adjustments have been made, all adverse information Zopa recorded about this loan should be removed from Mr S' credit file.

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

My final decision

For the reasons I've explained, I'm upholding Mr S' complaint. Zopa Bank Limited needs to put things right in the way set out above.

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

Jeshen Narayanan
Ombudsman