

The complaint

Miss Z says Brent Shrine Credit Union Limited, trading as My Community Bank (MCB), irresponsibly lent to her.

What happened

Miss Z applied for a loan of £20,000 over 60 months from MCB on 20 September 2022. Her application was approved and she was offered a loan with an APR of 16.81% making the monthly repayments £482.44, and the total repayable £29,472.81.

Miss Z says she was already in financial difficulties when she applied and things have since got worse. Her credit report would have shown her late payments and she was constantly overdrawn. She has struggled every month to keep up with the payments and cannot get out of her overdraft. She has had to borrow from family and friends to pay her priority payments such as bills and rent. The financial stress has severely affected her mental health.

MCB says it carried out appropriate creditworthiness and affordability checks and these showed the loan would be affordable for Miss Z.

Our investigator upheld Miss Z's complaint saying MCB ought to have realised the loan would not be sustainably affordable. MCB disagreed and asked for an ombudsman's review. It said, in summary:

- The Open Banking data included a lot of transfers in and out of Miss Z's account so it was not a realistic representation of her finances. It therefore used national statistics from the ONS to estimate her housing and living costs.
- Using her actual income from the Open Banking data and deducting outgoings on that basis (with a £50 buffer), plus her existing credit commitments from its credit check, meant it calculated Miss Z had monthly disposable income of £639.33 and so could afford to take on this loan.
- Accepting Miss Z was overdrawn, she also had savings at the time and her overdraft limit was very low relative to her income, and a free line of credit.

As a Credit Union, its specialist sourcebook is the Credit Union sourcebook (CREDS) not the Consumer Credit sourcebook (CONC). Its loan agreements are unregulated. But, it said, as a credit union which exists for its members, it applies a fair and reasonable lending policy and treats its customers fairly. Its standard lending criteria were applied in this case and they align with good industry practice.

I reached the same conclusion as the investigator but made some different findings in places so I issued a provisional decision to give both parties a chance to respond before I made a final decision.

An extract from my provisional decision follows and forms part of this final decision. I asked both parties to send any comments or new evidence by 10 April 2024.

Extract from my provisional decision

In its response to the investigator's assessment MCB flagged that its loan agreements are exempt and not subject to the rules and guidance set out in CONC.

I agree. MCB is a credit union regulated by the Financial Conduct Authority (FCA). The FCA's Credit Unions Sourcebook (CREDS) sets out the FCA's regulatory rules and guidance which apply to credit unions. Credit unions are registered under the Co-operative and Community Benefit Societies Act 2014 and operate under the Credit Unions Act 1979. Generally speaking, their loan agreements are exempt from the application of the UK's general consumer credit regime and are not regulated credit agreements. Save in exceptional circumstances, their lending activities do not fall within the FCA's definition of a "credit-related regulatory activity" and so these activities are not subject to any of the rules and guidance in the FCA's Consumer Credit sourcebook (CONC) including rules and guidance on responsible lending.

I want to reassure MCB I have solely focussed on the rules and guidance in CREDS which do apply in this case, as well as the credit union's own stated lending policy to treat all customers in a fair and reasonable manner.

Of particular relevance is CREDS 7.2.1AR that states "A credit union must establish, maintain and implement an up-to-date lending policy statement approved by the governing body that is prudent and appropriate to the scale and nature of its business." And CREDS 7.2.6G that states "The lending policy should consider the conditions for and amounts of loans to members, individual mandates, and the handling of loan applications."

In other words, the FCA requires that MCB's lending policy should be prudent, and should be applied in a manner which protects MCB's members as a whole.

To decide this complaint I have therefore looked at the checks MCB carried out, assessed whether these allowed it to meet its obligations and considered, if not, what adequate checks would have most likely shown.

MCB carried out an affordability assessment and creditworthiness check when Miss Z applied for her loan. I've reviewed the information it relied on to make its lending decision.

It has told us this included Miss Z's income. The final response letter said this was verified with one of the credit reference agencies, but more recently in response to the investigator's assessment it implied it used verified actuals from Open Banking data. It used estimates for her housing and living costs using national statistics, and the results of a credit check it carried out to understand the monthly cost of her existing credit commitments. It added a £50 buffer to her expenses. I cannot see it asked about the purpose of the loan – Miss Z has subsequently told us it was for debt consolidation. From these checks combined MCB concluded Miss Z had monthly disposable income of £639.33 and so could afford this loan with its monthly repayment of £482.44.

I am not satisfied these checks were adequate. Miss Z was looking to borrow a large amount of money over a five-year term. So to treat her fairly MCB needed to know she could do this without suffering any financial harm over that extended period of time. And I think this meant it needed to do a fuller financial review based on her actual outgoings.

It argues that the Open Banking data was not representative of her financial position as it included multiple transfers in and out so it did not use it to make its lending decision. But I think it would have been a useful starting point – although given the information in that report I would have still expected MCB to then carry out further checks. I say this as there were

several concerning entries – most critically four ‘possible missed payment’ entries - three on priority bills. There were also multiple Buy Now Pay Later transactions (totalling £987.45 in the month prior to application) which could, though not always, suggest financial strain. And it seemed Miss Z’s housing costs were four times higher than the lender’s estimate. It was not fair on Miss Z for MCB not to respond to this information.

In cases like this we look at bank statements for the three months prior to application. I am not saying MCB had to do exactly this but it is a reliable way for me to understand what better checks would most likely have shown. From the extracts Miss Z has provided I can see Miss Z was under financial pressure – she was persistently reliant on her overdraft facility, even after payday. This was not a free line of credit as MCB argues – she was incurring fees for the use of her arranged facility but also for unarranged use. There were returned direct debits with charges too.

I have considered the loan was for debt consolidation but I have seen no evidence that MCB knew this, or that it had taken steps to understand which debts Miss Z intended to settle to ensure this loan would be financially helpful to her. There was also, I feel, a red flag in that Miss Z was applying for an amount that was much higher than the level of debt MCB understood she had – again an area that merited investigation.

I accept MCB’s point that the number of transfers in/out of Miss Z’s account makes it hard to truly understand her financial position. But that in itself confirms to me that it did not have the assurances it needed before lending that the loan would not cause financial harm to Miss Z. And unless MCB can evidence that it knew Miss Z was planning to clear her overdraft I don’t find it was fair to lend to her. If she stayed dependent on that facility, and continued not to use it for the short-term support it is designed to provide, I cannot fairly conclude this loan was not financially harmful for Miss Z. Indeed, I note that she remained reliant on her overdraft in the months following receipt of this loan.

In addition, taking a slightly different approach to the analysis of the lending decision and assuming Miss Z repaid all her unsecured debt, I still cannot find MCB acted in a fair or reasonable way towards Miss Z. MCB learnt from the Open Banking data that Miss Z’s mortgage cost was £800. Using that figure in its affordability assessment - with actual salary data and ONS data for living expenses - would not have shown this loan to be affordable.

In the round I cannot fairly conclude that MCB made a fair lending decision. There were clear indicators that Miss Z would struggle to repay this loan. I find that by lending to her MCB failed to both treat her fairly in line with its stated policy, and to protect its members as a whole as required.

I then set out what MCB would need to do to put things right.

Miss Z replied by the deadline accepting my provisional decision. MCB did not respond.

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 set out above I have considered the actions of MCB in the context of the rules and guidance in CREDS, as well as the credit union’s own stated lending policy to treat all customers in a fair and reasonable manner.

As neither party submitted any comments or new information for me to consider I have no grounds to change the findings or conclusion in my provisional decision.

It follows for the reason set out above I find MCB was wrong to lend to Miss Z.

Putting things right

As I don't think MCB should have arranged this loan, I don't think it's fair for Miss Z to pay any interest or charges for the borrowing. However, Miss Z did have the use of the funds she was lent, so I think it's fair she repays them.

This means to settle Miss Z's complaint MCB must:

- remove all interest, fees and charges from Miss Z's loan account and treat all repayments Miss Z has made as repayments of the capital
- if this results in any overpayments they should be refunded adding 8% simple interest per year* from the date of each overpayment, if there were any, to the date of settlement
- if this means Miss Z hasn't repaid the capital amount lent then MCB should arrange an affordable payment plan for the shortfall
- remove any adverse information recorded on Miss Z's credit file regarding the agreement, once any outstanding balance has been repaid.

*HM Revenue & Customs requires MCB to take off tax from this interest. MCB must give Miss Z a certificate showing how much tax it's taken off if she asks for one. If it intends to apply any refund due to reduce the capital balance it must do so after deducting the tax.

My final decision

I am upholding Miss Z's complaint. Brent Shrine Credit Union Limited, trading as My Community Bank, must put things right as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Miss Z to accept or reject my decision before 9 May 2024.

Rebecca Connelley
Ombudsman