DRN-4830715

The complaint

Ms T complains that Specialist Motor Finance Limited (SMFL) approved a Hire Purchase agreement for her without completing sufficient affordability checks.

What happened

In October 2019, Ms T acquired a used car financed through an agreement with SMFL. The cash price of the car was £12,080. Ms T paid a cash deposit of £94 with the balance of £11,986 provided as credit through the agreement.

The agreement required Ms T to make 59 monthly repayments of £361.95, followed by a final repayment of £371.95 on month 60. Ms T settled the finance in May 2022, ending the agreement early.

In July 2022 Ms T complained to SMFL that their decision to lend to her was irresponsible and the finance should not have been agreed. SMFL didn't think they'd done anything wrong and said based on what they knew about Ms T's circumstances, they believe they acted fairly and responsibly in providing the finance.

SMFL said Ms T informed them she was earning £1,850 per month which they verified as being accurate and they completed a check of her credit history. SMFL also said they deducted from Ms T's income, amounts for the cost of living based on her having told them she was single at the time, living with her parents, and her existing credit commitments.

Finally, SMFL said, while their calculations left Ms T with a disposable income of around £940 a month, to ensure the agreement was affordable, the maximum monthly payment they would agree to was set at £362.

Ms T remained unhappy, so she asked the Financial Ombudsman Service to look into her complaint.

Our Investigator looked into things, but she didn't think based on the information SMFL saw, they'd completed proportionate checks to determine Ms T's disposable income at the time.

Our Investigator said the credit check results provided by SMFL showed she'd made late payments to her existing credit commitments, was close to agreed credit and store card limits and had exceeded an agreed overdraft limit at the time. Further, she said the credit check results also confirmed Ms T was in an arrangement to pay on two accounts and confirmed the presence of a debt management plan on another.

Considering Ms T's circumstances and the borrowing in question, alongside what SMFL found out about her financial history, our Investigator didn't think using statistical data to determine her expenditure was reasonable and that SMFL should've done more.

Our Investigator went on to consider what SMFL would most likely have found had they done reasonable and proportionate checks. To do this she looked at Ms T's bank statements, a copy of her credit report and her debt management plan.

Our Investigator said she could see Ms T had a personal loan commitment for £487 a month which differed to an amount of £18.25 a month recorded by SMFL, as well as other commitments she couldn't see they'd taken into consideration. She thought had they done it wouldn't have left Ms T with enough disposable income to sustainably afford the monthly repayments for the duration of the term.

To put things right our Investigator said SMFL should refund all interest and charges paid by Ms T, adding 8% simple interest from the date of the payments to the date of settlement and remove any adverse data regarding the original agreement from her credit file.

SMFL questioned the personal loan commitment discrepancy saying the balance shown on the credit report they received at the time indicated the loan was ending. SMFL asked for copies of Ms T's bank statements and debt management plan for them to review and provide comment.

Our Investigator shared the credit report obtained from Ms T which showed the personal loan commitment continued until February 2021 along with bank statements and a copy of Ms T's debt management plan. SMFL didn't respond further.

As no resolution could be reached, this case has been passed to me to decide.

I sent Ms T and SMFL my provisional decision on 17 May 2024. I explained that whilst I'd reached to same outcome as out Investigator, my reasoning is not quite the same.

Prior to issuing this provisional decision, I asked SMFL to provide me with any comments regarding the documentation provided to them, if they remained in disagreement with our Investigator's view. I've not received a response. In my provisional decision I said:

'How we handle complaints about irresponsible and unaffordable lending is explained on our website. It's this approach I've used when deciding Ms T's complaint. SMFL needed to ensure they didn't lend irresponsibly which in practice, means they needed to carry out proportionate checks to be able to understand whether any lending was affordable and sustainable for her before agreeing to provide the finance.

The rules that apply to credit agreements are set out in the FCA's consumer credit sourcebook (CONC). Section 5.2A of CONC is relevant here, as – among other things – it talks about the need for businesses like SMFL to complete reasonable and proportionate creditworthiness assessments before agreeing to lend someone money.

I've considered these rules by asking the following questions:

Did SMFL complete reasonable and proportionate checks to satisfy themselves Ms T would be able to meet the repayments of the borrowing without experiencing significant adverse consequences?

- *If they did, was their decision to lend to Ms T fair?*
- *If they didn't, would reasonable and proportionate checks have shown that Ms T could sustainably repay the borrowing?*

<u>Did SMFL complete reasonable and proportionate affordability checks?</u>

What's considered reasonable and proportionate in terms of the checks a business undertakes will vary dependant on the details of the borrowing and the consumer's specific circumstances at the time.

Here, the total amount repayable under the agreement was over £21,800, with monthly repayments of around £360 over a 60-month term. The annual percentage rate charged by SMFL was 29.9%. This was therefore a significant and lengthy credit commitment for someone to enter into, so my starting point is that I'd expect to see SMFL to have completed a thorough affordability check.

SMFL say relevant checks were completed because they assessed Ms T's application by reviewing data taken directly from her and from credit reference agencies, alongside using statistical data to calculate her income and expenditure, and ultimately determine her affordability to meet the repayments.

They arrived at a monthly income of £1,850, living costs of around £780 a month and payments to existing creditors of around £100 a month. After then deducting a buffer of £25 a month, SMFL said Ms T's disposable income was around £940 a month.

CONC allows firms to use statistical data in their affordability assessments unless they have reason to suspect that a customer's non-discretionary expenditure is significantly higher than that described in the data, so I've thought about what SMFL knew from the checks they did do.

While SMFL have not been able to provide me a copy of the credit report itself, they have provided me a summary of what they say they saw at the time of the application. I can see they saw Ms T had a total of ten active credit accounts including two unsecured loans and four credit cards or store cards, of which she'd utilised over 85% of the combined credit limits at the time. Ms T was also over her agreed overdraft credit limit on one current account at the time.

I can also see they saw Ms T had missed multiple payments on one credit or store card in the immediate months prior to the agreement in question. The credit check results provided by SMFL also indicated Ms T was in an arrangement to pay on one credit or store card and one communications account at the time and had a further credit card or store card that was subject to a debt managed programme.

SMFL said due to them offering a 'Sub-Prime' product, it's not unusual for them to see missed payments and/or defaults on applicants' credit files and Ms T's credit file didn't give them any cause for concern. But I think all of the above are indicators that Ms T might have been in some financial difficulty and therefore that her expenditure might be significantly higher than SMFL had estimated.

Overall, on balance I'm not satisfied SMFL did proportionate checks and I think they should have done more to understand her financial situation and her specific expenditure given the credit check results they saw.

<u>If SMFL had carried out proportionate checks, what would they have found?</u>

I can't be sure what information and evidence SMFL would've asked for or received had it carried out a reasonable and proportionate check but as I've said above, I think it would have involved them finding more out about Ms T's financial circumstances and expenditure at the time.

SMFL say they were told by Ms T she was living with her parents at the time of the application and had no dependants, so they split rent and cost of living estimates when calculating her disposable income.

As I've explained above, SMFL based their income and expenditure calculations on Ms T *earning a net monthly income of £1,850. They then deducted an amount of around £780 to the cover cost of living and around a further £100 to cover her existing credit commitments. SMFL also allowed for a buffer of £25 before calculating the maximum monthly repayment they would agree.*

To determine what else SMFL might have found if they'd done more checks, I've considered what Ms T has told us carefully, alongside looking at her bank account statements for the three months leading up to her application, her credit file and a copy of her debt management plan.

Having done so, I can see Ms T received an average monthly income from her employer of around £1,720.

Ms T's non-discretionary monthly expenditure was on average £1,292, consisting of around £350 for food, £134 on insurance and transport, £214 towards communication accounts, £54 on subscriptions and account fees and £540 towards short term financial commitments.

This left her with an average disposable monthly income of around £428 per month. After including the monthly commitment of around £360 for the loan from SMFL, this left Ms T with a disposable income of around £66 a month. I'm not satisfied this was a sufficient amount of funds left available to demonstrate the borrowing would be sustainably affordable going forward.

In my calculations above I've not included payments to either the personal loan with a commitment of £487 or the repayment to the debt management plan mentioned by our Investigator. I'll explain why.

While her credit report does show Ms T had a personal loan with a monthly commitment of £487 which ran until March 2021 and Ms T's provided a copy of her debt management plan, I've not seen any regular repayments being made via her bank account statements to support that she had an ongoing commitment towards them.

That said, I can see Ms T received two payments from a third party totalling £15,000 in July 2019. Ms T's explained to us that this was a loan from a relative for the purpose of her being able to pay off some of her debt and exit her debt management plan.

I can see Ms T paid around £7,500 towards the personal loan and around £4,850 towards her debt management plan shortly after receiving the funds, so I'm satisfied this supports her testimony. And while I can't say she has a committed repayment to make to her relative, I think SMFL would have seen this amount credit her account and ought to have done more to find out the circumstances behind it.

So, in summary, I'm satisfied had SMFL done more to understand Ms T's non-discretionary monthly expenditure, they ought to have realised the borrowing was neither affordable or sustainable and as such wouldn't have agreed to lend to her.

But my role isn't solely to decide if the borrowing in question was affordable or not. I must also consider if SMFL acted responsibly by agreeing to provide credit to Ms T and I'm not satisfied they did. I'll explain why.

Ms T's bank account statements show she was heavily reliant on short-term pay day loans to subsidise her income. Over the three-month period in question, nine payments credited her account totalling around £1,100.

Ms T was also heavily reliant on her overdraft on one of her accounts, only returning into *credit briefly on occasions before moving straight back into debt. And despite having the overdraft facility in place, 20 direct debit commitments were unpaid over the three-month period.*

In addition, Ms T has told us she was fighting a gambling addiction at the time of taking out the finance. While I'm not saying she told SMFL this at the time, I think had SMFL done more to find out about her circumstances, it would've been clear her gambling spending was compulsive and not under control. I say this because Ms T made 121 gambling transactions over the three-month period spending a total of £4,647.

I think this ought to have demonstrated to them it was irresponsible to grant the finance to Ms T and that she would struggle to maintain the repayments sustainably throughout the full term of the agreement.

So, in summary I don't think SMFL completed proportionate checks prior to lending to Ms T, and I think had they done, what they'd have found out would've led them to decide Ms T was neither in a position to sustainably repay the agreement, nor was it responsible to grant her the lending.

I don't think SMFL made a fair lending decision by approving the agreement they did.

Putting things right

As I don't think SMFL should've lent to Ms T, I don't think it's fair for them to be able to apply any interest or charges under the agreement. So, Ms T should only have to pay the original cash price of the vehicle, that being £11,986.

SMFL should refund any payments Ms T has made in excess of £11,986, adding 8% simple interest per year from the date of each overpayment to the date of settlement.*

Finally, SMFL should remove any adverse information recorded to Ms T's credit file in relation to this agreement.

**If SMFL consider that they're required by HM Revenue & Customs to take off income tax from any interest due to Ms T, they should tell her how much they've taken off. They should also give Ms T a certificate showing this if she asks for one, so she can reclaim the tax from HM Revenue & Customs if appropriate.'*

Ms T accepted my provisional decision. SMFL requested copies of Ms T's bank statements again however neither accepted nor challenged my provisional decision.

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 neither party had provided anything further for me to consider following my provisional decision, I've seen no reason to reach a different conclusion to the one I reached previously. For the reasons set out above in my provisional decision, I've decided SMFL need to do the following to put things right.

Putting things right

As I don't think SMFL should've lent to Ms T, I don't think it's fair for them to be able to apply any interest or charges under the agreement. So, Ms T should only have to pay the original cash price of the vehicle, that being £11,986.

SMFL should refund any payments Ms T has made in excess of £11,986, adding 8% simple interest* per year from the date of each overpayment to the date of settlement.

Finally, SMFL should remove any adverse information recorded to Ms T's credit file in relation to this agreement.

*If SMFL consider that they're required by HM Revenue & Customs to take off income tax from any interest due to Ms T, they should tell her how much they've taken off. They should also give Ms T a certificate showing this if she asks for one, so she can reclaim the tax from HM Revenue & Customs if appropriate.

My final decision

For the reasons I've given above, I uphold Ms T's complaint. Specialist Motor Finance Limited should do as I've set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Ms T to accept or reject my decision before 1 July 2024.

Sean Pyke-Milne
Ombudsman