

The complaint

Mr and Mrs Y complain that Evolution Lending Limited irresponsibly lent them a second charge mortgage (secured loan).

What happened

Mr and Mrs Y have taken out a series of secured loans with Evolution – in September 2016, April 2017, June 2018 and September 2021.

- Loan 1, September 2016 – Mr and Mrs Y borrowed £9,144 for debt consolidation and home improvements. This loan was replaced with loan 2.
- Loan 2, April 2017 – Mr and Mrs Y took this loan out to repay loan 1, borrowing £17,800. Mr and Mrs Y refinanced this loan with a different lender in March 2018.
- Loan 3, June 2018 – Mr and Mrs Y borrowed £12,000 plus £1,899 fees over 15 years for debt consolidation and to finance replacing their central heating system. The interest rate was 26.82% variable, giving an initial monthly payment of £286.08. Mr and Mrs Y refinanced this loan when they re-mortgaged their main mortgage in August 2021.
- Loan 4, September 2021 – Mr and Mrs Y borrowed £10,000 plus £1,699 fees over 10 years for debt consolidation. The interest rate was 19.56% variable, giving an initial monthly payment of £210.80. Mr and Mrs Y refinanced this loan with a different lender in September 2022.

In 2023 Mr and Mrs Y complained that all four loans had been mis-sold. Their representative said that their financial history at the time showed they were wholly dependent on credit, and that their overall borrowing was becoming unsustainable. While they hadn't missed any payments on their Evolution loans, they had a history of arrears across other lending and had taken out a series of secured and unsecured debts. They were in a spiralling situation of relying on credit card and catalogue debt to finance their daily living costs, because their income was taken up with other debt repayments – which in turn increased their indebtedness and monthly outgoings. The very large fees, and high interest rate, charged by Evolution only made matters worse. In lending to them, Evolution only made their situation worse.

Evolution said that we couldn't consider the complaints about loans 1 and 2, because they had been made out of time. It said that it had made proper checks to establish that loans 3 and 4 were affordable for Mr and Mrs Y and hadn't irresponsibly lent to them. It said it had checked income and expenditure using payslips and bank statements, as well as checking their credit files. It said that Mr and Mrs Y hadn't missed any payments during any of the loans, and hadn't suggested at any point that they were struggling, or asked for forbearance.

Our investigator didn't think the complaint should be upheld in respect of loans 3 and 4 – loans 1 and 2 being out of time. He said that they reduced Mr and Mrs Y's outgoings, which improved their overall position. Mr and Mrs Y's representative asked for an ombudsman to

decide the complaint.

My provisional decision

I reached a different view, so I issued a provisional decision. I said:

“Loans 1 and 2

As our investigator explained, we can't consider complaints about events that took place more than six years before the complaint, and where the complaint is made more than three years after the complainant knew, or ought reasonably to have known, of cause for complaint – unless there are exceptional circumstances. Evolution hasn't consented to us looking at an out of time complaint about these loans and Mr and Mrs Y's representative accepts that we can't do so. In the rest of this decision, therefore, I'll focus on the later two loans.

Loan 3

Evolution obtained Mr and Mrs Y's payslips. It recorded Mr Y's pay as being £1,238 per month – this is the average of the three payslips it obtained. But two of those months showed basic pay of £1,156 – with the third including overtime of £1,402. I'm not persuaded it was reasonable to include this overtime element when calculating Mr Y's regular pay.

The same approach was taken with Mrs Y's payslips – Evolution used the average of £1,657, though the three months were £1,701, £1,571 and £1,699. Again, I'm not persuaded that it was reasonable to use the average to calculate regular pay when that was reliant on overtime and one of the three months – even with overtime – was well below that figure.

Evolution stress tested Mr and Mrs Y's main mortgage and this loan, applying an uplift of 1.66% for the main mortgage and 1% for this loan. That resulted in a stress test value of £41.59. Given that the recommendation in the mortgage rules was for a stress test of 3% on both loans, and Evolution hasn't explained why it didn't follow that recommendation, I'm not persuaded this was reasonable.

The total income Evolution recorded was £2,985 and the total expenditure was £2,588 per month. Reducing the income figures to £1,156 for Mr Y and £1,571 for Mrs Y brings the income down to £2,727. Applying a 3% stress test would add around £100 per month to the expenditure – bringing it to around £2,690. I'm not persuaded that with such a small gap between income and expenditure Evolution had a proper basis for concluding that this loan was affordable for Mr and Mrs Y.

Loan 4

The income and expenditure assessment completed at the time shows employed income for both Mr and Mrs Y, together with child benefit, giving a total income of £3,355 per month. The income for Mrs Y is consistent with the May and June 2021 payslips Evolution obtained. The July payslip shows a significantly lower income because of a period on statutory sick pay.

By this time, Mr and Mrs Y had a great deal of unsecured debt, most of it in Mrs Y's name. They consolidated three separate loans paid off directly by Evolution. Mr and Mrs Y retained a number of other loans and credit cards. As well as the monthly payments to the Evolution loan, the monthly payments to the retained unsecured

credit were recorded as exceeding £1,000.

The affordability assessment showed a surplus of around £400 per month. But I think this is likely to have been an underestimate. Not only were there potential issues with Mrs Y's income, but also Evolution has confirmed that it stress tested their main mortgage and this loan at 2.25% rather than the 3% recommended by the rules of mortgage regulation. It's not clear why it used a lower figure, and in the absence of a good reason I don't think it was fair to use a lower percentage.

I think Evolution also ought to have been concerned about whether the lending was sustainable. Mr and Mrs Y had taken out a series of secured loans in the past, consolidating unsecured debt, running up more debt and consolidating again. They'd just re-mortgaged to pay off the last Evolution loan – but had increased the balance of the main mortgage from £55,000 to £91,000, much more than was needed just to pay off the Evolution loan. Yet despite this substantial increase in their secured indebtedness they were looking to take yet another secured loan, for further debt consolidation, just a month or so later – while leaving still more unsecured debt unconsolidated. I think this shows a clear pattern of worsening indebtedness, leading to increased secured lending, leading to further indebtedness. I'm not persuaded it was reasonable to conclude this was likely to be sustainable or that it was responsible to lend.

Putting things right

I've said that I'm not persuaded that Evolution ought to have lent either of these loans. I therefore need to think about what it should do to put matters right. I think it's relevant to take into account that while there may have been issues with the lending decisions both loans were paid off in full (albeit relatively early into their terms), and that Mr and Mrs Y didn't miss any payments while they were in place.

In both cases, Mr and Mrs Y replaced these loans with other secured lending – in both cases not just consolidating these loans but also taking further borrowing. I've seen both their credit files (both from now and from the time of the lending), and they show a consistent pattern of taking out substantial amounts of secured and unsecured debt, consolidating and re-financing and then further increasing their indebtedness.

I'm not persuaded in the circumstances of this case that it would be fair and reasonable to require Evolution to repay the interest it charged on these loans. While Mr and Mrs Y wouldn't have paid that interest if Evolution hadn't lent to them, given what I've seen of the history I'm satisfied it's more likely than not they'd have sought to borrow somewhere else instead – and the consolidated loans were interest bearing before consolidation. I don't think it's likely Mr and Mrs Y would have looked to come to an arrangement with their creditors, for example, given their pattern of shifting and consolidating debt over many years. On balance, I think it's more likely than not that if Evolution hadn't lent to them Mr and Mrs Y would have tried to apply for similar loans elsewhere – and if unsuccessful (on the basis that, acting fairly, other lenders would have had the same concerns I've found Evolution should have had) I think it's most likely would have retained their unsecured debt until they were able to re-finance.

I also need to bear in mind that, in both cases, Mr and Mrs Y didn't miss any payments while they had the loans, and that both were later re-financed as part of their pattern of shifting debt. While I've found that the loans weren't responsibly lent, for the reasons I've given above, it's relevant that they were not so unaffordable that

Mr and Mrs Y were caused substantial detriment before repaying them. I also bear in mind that these loans are not still outstanding and Mr and Mrs Y therefore aren't currently being required to pay interest to service them. I think that, in the particular circumstances of this complaint, if I were to require Evolution to refund interest charged on this borrowing – on the basis that it shouldn't have charged interest on lending that should never have been granted – that would leave Mr and Mrs Y better off than they would otherwise have been and risks over-compensation.

However, because I don't think they ought to have been lent I think it would be fair and reasonable to require Evolution to refund the fees charged when they were taken out. Those fees were charged to access loans that weren't responsibly lent and, in part, charged to cover Evolution's costs in assessing whether to lend. I also think it's highly relevant that the fees were substantial, and substantially increased the amount Mr and Mrs Y owed overall. Those fees remain part of their outstanding debts elsewhere now. While I haven't found it would be fair for Evolution to refund interest they would likely have paid elsewhere instead, I don't think it's fair that their ongoing indebtedness has been increased by the fees charged for lending that shouldn't have been granted."

The responses to my provisional decision

Evolution said it had nothing further to add.

Mr and Mrs Y's representative agreed that the complaint should be upheld, but didn't think I had proposed fair redress. It said that I ought fairly to require Evolution to refund the interest it charged as well as the fees, because:

- The case of *Kerrigan v Elevate Credit*¹ set a precedent that a full refund of interest should be made in cases of irresponsible lending. This puts the borrower back in the position they would be in had the loan never been issued, deters lenders, and mitigates the financial harm caused by increased indebtedness.
- Evolution fell short of the FCA's Principles, which warrants a full interest refund.
- The CONC rules provide guidance on responsible lending, which Evolution failed to meet.
- The DISP rules require a firm to take appropriate action to correct wrongs.
- The loans were mis-sold, and so Mr and Mrs Y should not have paid any interest to Evolution – which should therefore refund it in full.

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.

Having done so, and having considered the responses to my provisional decision, I haven't changed my mind about the fair way to put things right in the particular circumstances of this complaint.

The CONC rules – the regulator's rules for consumer credit lending – aren't relevant to this

¹ *Kerrigan and others v Elevate Credit International Limited (t/s Sunny) (in administration)* [2022] EWHC 2169 Comm

complaint. As a complaint about regulated second charge mortgage lending, the relevant rules are in MCOB, not CONC, and I took full account of what MCOB says in making my provisional findings. Both MCOB and CONC set out what firms should do when considering whether to lend mortgage and consumer credit lending respectively – but neither prescribe redress for complaints which are upheld. Nor does DISP – beyond requiring me to decide a complaint by what I consider to be fair and reasonable in all the circumstances.

I've taken the *Kerrigan* case into account. That complaint was about short-term unsecured lending, not mortgages. In that case, the court said that in such cases the refund of interest and charges was likely to be appropriate redress for irresponsible lending. But that ultimately any redress would depend on the facts of the individual case.

In reaching my provisional decision, I did take into account the facts of this individual case. As I explained, I wasn't persuaded that either loan three or loan four caused any detriment – there were no missed payments, and while fees added to the loan increased Mr and Mrs Y's indebtedness, I said those fees should be refunded. I agree that it's reasonable to say that, as a starting point, Evolution should not have charged – and should not retain – interest on loans it should never have lent. But as I also said in my provisional decision, both loans were used to repay debts that Mr and Mrs Y already had. Had the loans not been granted, they would have retained those other debts (or re-financed them in other ways).

Both loans were outstanding for relatively short times before being themselves re-financed; Mr and Mrs Y did not have any difficulty in making the payments while they had them; and they would have paid comparable interest elsewhere had these loans not been taken. In the particular circumstances of this complaint, therefore, I'm satisfied that Evolution caused Mr and Mrs Y detriment by charging them fees, added to the loan balances, which should not have been charged because the loans should never have been lent. That increased their indebtedness. But I remain of the view that refunding interest as well would, in the individual circumstances of this particular case, put them back in a better position than they would have been in had nothing gone wrong.

My final decision

My final decision is that I uphold this complaint and direct Evolution Lending Limited to:

- Refund £1,899 fees in respect of loan 3, adding compound interest at the loan rate from date of completion to date of redemption, and compound interest at the rate charged on Mr and Mrs Y's first charge mortgage (into which it was consolidated) from date of redemption to date of refund.
- Refund £1,699 fees in respect of loan 4, adding compound interest at the loan rate from date of completion to date of redemption, and compound interest at the rate charged by the new second charge lender which re-financed this loan from date of redemption to date of refund.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs Y and Mr Y to accept or reject my decision before 10 December 2024.

Simon Pugh
Ombudsman