The complaint

Mr and Mrs Z complain that Evolution Lending Limited irresponsibly lent them a second charge mortgage (secured loan). They also complain that it didn't treat them fairly when they later experienced financial difficulty and eventually had to sell the property.

What happened

In 2018 Mr and Mrs Z discussed taking out a secured loan with a firm called Evolution Money Limited, a sister firm of Evolution Lending. Evolution Money recommended that they take a loan with Evolution Lending to consolidate some of their existing unsecured debt.

Mr and Mrs Z borrowed £24,000, plus £3,099 in fees, over a fifteen year term. Interest was charged at a variable rate, initially 16.08%, giving a monthly payment of £379.26.

In 2019 Mr and Mrs Z missed a payment. In 2020, Mr Z's employment was impacted by the coronavirus pandemic and the loan fell into arrears. Mr and Mrs Z were unable to get things back on track and in 2024 they sold their property and repaid the loan.

In 2024 Mr and Mrs Z complained that Evolution hadn't lent responsibly. They also complained about how they were treated during their financial difficulties. Evolution said that it had considered their income and expenditure, checking payslips and bank statements, and established that the loan was affordable. It said they had no defaults recorded on their credit files and it had lent responsibly. The loan only became unaffordable because of later life events.

Evolution also said it had offered appropriate forbearance when Mr and Mrs Z got into difficulty. It said it had given them a payment deferral until June 2020, after which Mr and Mrs Z resumed making payments. But the November 2020 payment failed – Evolution tried to contact Mr and Mrs Z without success. Mr and Mrs Z made some payments between May and October 2021 but then stopped again. In January 2022 they asked for forbearance while they sold the property. Evolution said that a check of their income and expenditure showed Mr and Mrs Z could afford to make the payments. But then in February 2022 Mr Z lost his job. Evolution put a hold on further collections activity, and the loan was repaid when the property was sold in April 2024.

Our investigator said the complaint should be upheld – he didn't think Evolution had shown that, properly considered, the loan was affordable. But he didn't think Evolution had acted unfairly when Mr and Mrs Z fell into financial difficulties.

Mr and Mrs Z accepted that, but Evolution didn't. So the complaint comes to me for a final 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.

Mr and Mrs Z were referred to Evolution Money to discuss an application for a loan to consolidate their unsecured debts.

According to Mr Z's credit file, at the time of the application he had (in addition to the main mortgage on the property) the following credit commitments:

- A current account with a £5,000 overdraft limit (held jointly with Mrs Z) – although he had cleared the overdraft a month before this application, it had been consistently near the limit for over a year before that.
- A credit card with a limit of £3,100 and a balance over £3,000.
- A second credit card, also with a limit of £3,100 and a balance over £3,000.
- A credit card with a limit of £7,000 and a balance over £6,900.
- A credit card with a limit of £2,350 and a balance over £2,300.
- An unsecured loan with a balance over £17,000 and monthly payments of £512.

There were no defaults or missed payments on any of the credit commitments. But just before the application Mr Z had taken 11 cash advances on his credit cards, totalling around £1,750. He told Evolution Money that this was to buy a car for Mrs Z, but no expenditure on a second car was included in the income and expenditure assessment.

Mrs Z's credit file said she had the following commitments:

- An unsecured loan with a balance of £5,000 and monthly payments of £213.
- A credit card with a limit of £450 and a balance below £50.
- A credit card with a limit of £6,550 and a balance, over the limit, of £6,598. The balance had been consistently at or over the limit for over a year.
- A credit card with a limit of £6,050 and borrowing that had been consistently at the limit for over a year.
- A credit card with a limit of £5,500 and a balance at the limit – this card had only been taken out at the end of 2017 and within three months had reached the limit.

Mr and Mrs Z's total unsecured debt exceeded the loan amount. Evolution Lending assessed the application on the basis that the two unsecured loans – totalling around £22,000 – were to be consolidated. This left the remaining debts as outstanding credit commitments.

Evolution had Mr and Mrs Z's joint current account statement for the month before the application, which showed that Mr and Mrs Z were paying more than the minimum payment to some of their credit cards. But it still only took into account a notional minimum payment of 3% of the outstanding balance when calculating their expenditure on credit commitments. This gave it a total (excluding the mortgage and the consolidated loans) of around £818 per month.

Evolution said it was reasonable to take into account only the minimum required payment, because those were payments only shown on one month's bank statement, and if Mr and Mrs Z paid those amounts each month the cards would soon be paid off – so this wouldn't be a long term commitment. And it said that it's reasonable to expect Mr and Mrs Z to prioritise secured debt over unsecured debt – to expect them to reduce their payments to credit cards to ensure this lending is affordable.

I'm not persuaded by this argument. Reducing credit card repayments to the minimum can make that form of borrowing very expensive, and mean it takes a long time to clear. If the only way for this loan to be affordable would be for Mr and Mrs Z to do that, then it's questionable whether the borrowing is sustainable or whether it's in their best interests to lend on that basis.

I also think that Evolution underestimated Mr and Mrs Z’s expenditure on credit commitments. It – rightly – noted that they had spent over £200 in the month before application on overdraft fees and interest. But it categorised this not as a credit commitment but as “non-essential expenditure”, and disregarded it entirely from the affordability assessment. Evolution says that this was because after consolidation just under £2,500 was paid to Mr and Mrs Z, which would have reduced their overdraft – and so the fees and interest.

That may be true – if Mr and Mrs Z used those funds for that purpose. But it’s not clear that they planned to or that they in fact did so. The overdraft was not included in the list of debts to be consolidated. And even if Mr and Mrs Z used the whole of the £2,500 to reduce their overdraft it would only have cut it in half, not repaid it altogether. So I don’t think it was appropriate to disregard the cost of their overdraft. It was a current credit commitment and – to a large extent – would have remained so after the lending, so should have been factored into the expenditure assessment.

I have other concerns about the expenditure recorded by Evolution too. For example, the property service charge is recorded as being £0.83 – it’s not clear if this is a monthly or annual figure, but given Mr and Mrs Z lived in a flat, that strikes me as being clearly implausible. There’s no figure recorded for ground rent either. I would have expected Evolution to have questioned this.

Evolution recorded expenditure on food as £655 per month, but the bank statement shows spending of over £800. Evolution recorded £50 on fuel, but the bank statement shows over £140.

Some of Mr and Mrs Z’s outgoings – notably gas / electric bills and service charge – aren’t on the bank statement at all. And the statement shows multiple transfers in and out to other accounts in Mr and Mrs Z’s names – almost 50 transactions, with a net movement out of over £2,000, over the course of the month. Evolution doesn’t appear to have questioned this or asked to see evidence of the other accounts.

Mr and Mrs Z’s main mortgage balance is recorded as being around £60,000 with a monthly payment of £249.38. This matches the information recorded on their credit files.

As part of the affordability assessment, the rules of mortgage regulation say that a lender should take into account the impact of future interest rate rises – known as a stress test. In the case of a second charge mortgage application, both mortgages should be stress tested.

At the time of the lending decision, the recommended stress test was 3% on the reversion rate. It’s not clear from Evolution’s file whether Mr and Mrs Z’s first charge mortgage was on a fixed rate or the reversion rate. If they were already on the reversion rate, a 3% increase in the interest rate would add around £150 to the monthly payment – this would be higher if they were on a fixed rate below the reversion rate.

The monthly payment on the Evolution loan was around £380. That loan was on a variable rate. Adding 3% to the interest rate would add around £67 to the monthly payment.

This gives a total stress test figure of around £217 – but Evolution only included £97 (£61 on the first charge mortgage and £36 on its loan). It’s not clear to me why it used such a low figure in the stress test. While the mortgage rules only require lenders to have regard to the 3% recommendation, in my view it’s good practice to do so and I’d expect to see good reason for departing from it.

On income, Evolution used a figure of £3,451.54 as Mr Z's net monthly income (plus £96.73 child benefit paid to Mrs Z). Mr Z was paid weekly, and his income varied considerably. Evolution said it took an average of the payslips provided (six months' worth) to arrive at that figure. I think that's a reasonable approach – but using the same payslips I have calculated an average of £3,327, so it's not clear to me how Evolution derived the higher figure.

Evolution calculated affordability like this:

- Income - £3,540
- Expenditure after consolidation - £2,545
- Evolution loan - £379
- Stress test - £97
- Disposable income - £519

However, using the figures I've found for income, expenditure and stress test, the calculation looks like this:

- Income - £3,423
- Expenditure after consolidation - £2,545
- Additional expenditure on food and fuel as per the bank statements - £255
- Overdraft interest and charges - £210
- Evolution loan - £379
- Stress test - £217
- Disposable income – negative £183

That is before taking into account any expenditure on service charges and ground rent, or what the transfers out of the current account might have been for, and doesn't factor in Mr and Mrs Z paying anything above the minimum on their credit cards each month. Taking all that into account, I'm not persuaded that this lending was, properly and fairly considered, affordable for them.

I'm also not persuaded that Evolution lent responsibly for other reasons. I think there's evidence that Mr and Mrs Z were overstretched and struggling with their existing commitments – in particular, their large overdraft and several credit cards at their limits suggest that. This lending consolidated the two large personal loans, but not the credit cards or the overdraft. While it reduced their overall outgoings, it still left them exposed to significant unsecured debt, additional secured debt, and at best marginal affordability. In those circumstances, it's difficult to conclude that there were reasonable grounds for concluding that the lending would be sustainable for Mr and Mrs Z.

For all those reasons, I uphold this complaint about the lending decision. I don't think, acting fairly, that Evolution ought to have lent to Mr and Mrs Z. To put things right, it should refund all the interest and fees they paid while the loan was outstanding. Because there is no outstanding liability, it should also remove the record of the loan from their credit files. But I don't require it to refund the capital they repaid, since Mr and Mrs Z benefitted from that in using it to clear some of their outstanding debts. And I don't require it to compensate them for any distress and inconvenience caused, because any compensation I would award is outweighed by the saving in interest resulting from the refund of interest charged on this account compared to interest saved by consolidating the unsecured loans. It's fair and reasonable that Evolution doesn't retain interest it should never have charged, and that Mr and Mrs Z aren't charged interest they should never have paid. But as that does result in a likely saving compared to the position they would have been in had the loan never been granted, requiring Evolution to pay separate compensation for distress and inconvenience is likely to result in over-compensation.

I’ve also thought about whether Evolution treated Mr and Mrs Z fairly when they experienced financial difficulty. I’m satisfied it did. It offered a payment deferral in 2020, and again in late 2020 / early 2021. When Mr and Mrs Z were unable to resume payments in 2021 after the deferral period, it tried to contact Mr and Mrs Z to discuss their situation, but without success. I’d expect a lender dealing with a customer in arrears to try and understand their situation and see what support could be provided, so this wasn’t unfair. Evolution also later didn’t take action while Mr and Mrs Z marketed and sold their property. Overall, I don’t think it acted unfairly in how it treated them over this period.

My final decision

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

- Re-calculate Mr and Mrs Z’s closing redemption balance as if:
    - The £3,099 fees had not been charged;
    - No interest had been charged for the life of the loan; and
    - All payments they made had been used to reduce the capital balance.
- Pay Mr and Mrs Z the difference between the actual and revised redemption figures, adding simple annual interest of 8% running from the redemption date to date of refund. If Evolution deducts income tax from the 8% interest element of my award, it should tell Mr and Mrs Z what it has deducted so they can reclaim the tax from HMRC if they are entitled to do so.
- Remove all record of this loan from their credit files.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr Z and Mrs Z to accept or reject my decision before 6 March 2025.

Simon Pugh
Ombudsman