

The complaint

Miss W complains that Evolution Lending Limited gave her a second charge loan without properly checking it was affordable for her and did not provide appropriate support when she experienced financial difficulty.

What happened

In 2019, Miss W received mortgage advice, which she accepted. She took a second charge loan secured against her home with Evolution for £20,000 with a product fee of £2,000 and a lending fee of £699 to be added to the loan. The term of the loan was ten years with a variable interest rate of 19.56%. The main purpose of the loan was to raise money to repay over £15,000 of unsecured debt.

Miss W considers that the loan was unaffordable and that Evolution did not carry out adequate checks before giving her the loan.

In 2022, the loan fell into arrears. Miss W does not consider that Evolution gave her sufficient support during the cost of living crisis and as a result the balance of the loan has increased and was higher than when she took the mortgage out. She wants Evolution to agree a fixed interest rate.

The investigator thought the complaint should be upheld. He said that Evolution had not carried out the correct stress test and if it had the loan would have been shown to be unaffordable. Even if that was not the case, Evolution had not accurately recorded Miss W's expenditure it would have identified the loan was not affordable or sustainable.

Evolution did not accept what the investigator said. It responded to make a number of points, including:

- It needed a breakdown of how the investigator had calculated Miss W's expenditure.
- It recorded £169 for food expenditure. And it accepted an explanation from Miss W that he spending on food and socialising was higher than declared because of a one-off event.
- Miss W gave a number of explanations about her spending and cash withdrawals and she was able to provide an acceptable explanation that they were not regular expenditure.
- It had applied a stress test. While it was not the 3% recommended by the Financial Policy Committee (FPC) that does not mean it was incorrect. It was only a recommendation.
- Miss W did not start to experience difficulty until the impact of the cost of living crisis was felt by her in 2022. So her difficulties were as a result of a change in her circumstances that could not have been foreseen. Before that she had managed her payments and had not told it about any issues.

- The evidence it had showed the loan was affordable and sustainable. It provided a clear benefit to Miss W – it cleared eleven items of credit and significantly decreased her monthly outgoings by around £370 a month. Had it not granted the loan it is likely Miss W's circumstances would have deteriorated and left her in a worse position.
- It was unreasonable for the investigator to include small day-to-day transactions in his calculation of expenditure. Most of those transactions were not committed or essential expenditure.

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.

Rules

The relevant rules in this case are the Mortgages and Home Finance: Conduct of Business sourcebook (MCOB). I must take those rules, amongst other things, into account in deciding what I consider to be fair and reasonable in the individual circumstances of this complaint. MCOB 11.6 covers responsible lending. Its requirements for lenders include:

- Before agreeing a mortgage, a lender must assess whether a customer will be able to pay the sums due under the mortgage and be able to demonstrate the mortgage is affordable.
- A lender must take full account of the net income of a customer, their committed expenditure, and the basic essential expenditure and basic quality-of-living costs of the customer's household.
- A lender may generally rely on any evidence of income or information on expenditure provided by a customer unless, taking a common-sense view, it has reason to doubt the evidence or information. A lender must have evidence of income and take reasonable steps to obtain details of a customer's committed expenditure. A lender can either obtain details of a customer's expenditure or use statistical data.
- If a lender is or should reasonably be aware from information obtained during the application process that there will, or are likely to, be future changes to the income and expenditure of the customer during the term of the mortgage, the lender must take them into account when assessing affordability.
- A lender must take account of the impact of likely future interest rate increases on affordability by applying a stress test. The lender must have regard to the prevailing FPC recommendation on interest rate stress tests, which at the time was 3%. This applies to all regulated mortgage contracts, not just first charge mortgages. A second or subsequent charge lender must also apply any stress test to the first and any subsequent charge loans as well as its own lending.

Affordability

Evolution recorded that Miss W had net income of £1,565.05 a month. I consider that was reasonable bearing in mind the evidence of her income that it had.

Evolution recorded that Miss W had expenditure of £1,346.63 a month including the Evolution loan. It said after stress testing the first and second charge loans Miss W would be left with £139.06 a month.

The investigator found that Evolution had under-recorded Miss W's expenditure. Evolution had bank statements from Miss W. They show that Miss W's expenditure was higher than

declared for food and socialising. Evolution accepted an explanation from Miss W that was due to on-off expenses. But I don't consider it was necessarily fair for Evolution to accept that explanation. While it had some evidence to support Miss W's expenditure it was not sufficient to verify her explanation. I can see that a responsible lender might have required bank statements covering a longer period.

Dealing with the stress test amount I do not consider Evolution has acted fairly and reasonably. Evolution has not told us the stress test percentage it used. It is lower than the FPC recommendation of 3%.

Evolution has told us that the FPC recommendation was "guidance not a ruling" – that is not quite correct. And it said it is "not regulated by the Prudential Regulation Authority". That is not relevant here. It is regulated by the FCA and it is required to follow MCOB. MCOB 11.6.18R (the "R" indicates it is a rule rather than guidance) says:

(1) Under MCOB 11.6.5R (4), in taking account of likely future interest rate increases for the purposes of its assessment of whether the customer will be able to pay the sums due, a mortgage lender must consider the likely future interest rates over a minimum period of five years from the expected start of the term of the regulated mortgage contract (or variation), unless the interest rate under the regulated mortgage contract is fixed for a period of five years or more from that time, or for the duration of the regulated mortgage contract (or variation), if less than five years.

(2) In coming to a view as to likely future interest rates, a mortgage lender must have regard to:

(a) market expectations; and

(b) any prevailing Financial Policy Committee recommendation on appropriate interest-rate stress tests;

and must be able to justify the basis it uses by reference to (a) and (b).

(3) For the purposes of this rule, even if the basis used by the mortgage lender in (2) indicates that interest rates are likely to fall, or to rise by less than 1%, during the first five years of the regulated mortgage contract (or variation), a mortgage lender must assume that interest rates will rise by a minimum of 1% over that period.

Evolution has not given us any evidence to show that it had regard to market expectations when applying the interest rate stress test it did. And while it is correct that the FPC only provided a recommendation on appropriate interest rate stress tests, there was still a requirement for Evolution to pay due regard to the recommendation in deciding what interest rate stress test to use. I don't consider Evolution has shown in this case that it did, in fact, pay due regard to the FPC's recommendation.

Evolution's response does not show that it understood the reasons why the FPC reached its recommendation or that it had sufficient reason to reasonably apply a different percentage stress test. It has not put forward any evidence that justifies its decision with reference to market expectations at the time or to show that it paid due regard to the FPC's recommendation. Therefore I do not consider Evolution has shown that it had sufficient reason to use a different stress test than that recommended by the FPC.

I understand Miss W was paying a variable interest rate on her first charge mortgage of 3.29%. She had a balance of around £63,000 – with £46,000 on an interest only basis and £17,000 on repayment over 12 years. Applying a 3% stress test would be an interest rate of

6.29% would increase the first charge payments by over £100 – rather than the £48 calculated by Evolution.

On the Evolution loan, a 3% stress test on the interest rate of 19.56% would be a rate of 22.56% and would increase payments by over £40 a month – rather than the £30.94 used by Evolution.

Therefore, if Evolution had used the 3% stress test it ought reasonably to have concluded that the loan was not affordable for Miss W. Applying the correct stress test Miss W's outgoings would exceed her income.

Evolution also had an obligation to pay due regard to Miss W's interests and to treat her fairly. A responsible lender acting reasonably ought to have known that there was a chance of harm to Miss W by securing previously unsecured debts against her property. It knew that she'd experienced payment difficulties and that she had to take an unsecured loan a few months earlier to pay for essential repairs to her home. There was sufficient reason for it to doubt the information Miss W had given about her expenditure. And if Evolution had applied the FPC's recommended stress test it could not reasonably have concluded the loan was affordable.

Overall, I do not consider that Evolution treated Miss W fairly when it approved the loan. I consider if it had done so it would have declined her application.

Support

Evolution was required to treat Miss W fairly when she experienced financial difficulty. It was reasonable for it to ask Miss W for details of her income and expenditure and for that to be updated from time to time. It was also not necessarily unreasonable for it to ask for bank statements to confirm her income and expenditure.

Without all of that information Evolution said it was not in a position to offer further support. Looking at all of the circumstances, and the level of engagement that might have been a reasonable stance for it to take. It said it would consider tailored support when it had that information. That ought to have included whether a concessionary interest rate was the right thing for Miss W. But it did not have enough information to consider what was an appropriate concession to offer.

In any event, Miss W has accepted the outcome proposed by the investigator – which I agree with – and that addresses the interest applied Evolution.

Putting things right

To put things right, Evolution should remove all interest, and the fees it charged, from the loan balance. It should treat all payments Miss W has made to date as being repayments of capital. It should then recalculate the outstanding balance.

If this results in a balance outstanding, Evolution should reach a sustainable arrangement with Miss W for the repayment of the remaining outstanding capital balance. If, however, this means that Miss W has already repaid more than the capital she borrowed, the excess should be refunded to her, adding simple annual interest of 8% running from when any payments above the total capital amount were made to the date Evolution refunds them. In this scenario, Evolution may deduct income tax from the 8% interest element of my award, as required by HMRC – but should tell Miss W what it has deducted so she can reclaim the tax if she is entitled to do so.

Evolution should also remove any adverse entries associated with this loan from Miss W's credit file.

I am not proposing an award for distress and inconvenience. That is because even if Miss W did not take this loan she would still have had to deal with her existing unsecured debts – and that would likely have caused a similar amount of distress and inconvenience as it did here.

My final decision

My final decision is that Evolution Lending Limited should take the steps set out above to settle this complaint.

Under the rules of the Financial Ombudsman Service, I'm required to ask Miss W to accept or reject my decision before 6 November 2025.

Ken Rose
Ombudsman