

The complaint

Miss S says that a secured (second charge) loan she took out in 2024 with UK Mortgage Lending Ltd trading as Pepper Money was unaffordable and irresponsibly lent.

What happened

Miss S applied for this loan through an independent mortgage broker. The offer issued on 9 August 2024 shows Miss S was borrowing £50,000 (plus £5,590 fees) over a 30-year term on a repayment basis. The interest rate was fixed at 14.258% for the first two years. That gave a monthly payment of £670.04.

The loan completed on 30 August 2024.

The January and February 2025 direct debits were returned as unpaid. The March 2025 payment was made, but it seems there was then no payment in April 2025 (which is the last update we have).

Miss S complained to Pepper about the loan in December 2024. Pepper issued a complaint response letter to Miss S on 22 January 2025. It said responsibility for the suitability of the advice and ensuring Miss S understood the product sat with the broker. It said it had asked about her recent time off work and the credit she had taken in recent months, and the responses were reasonable which didn't pose any further concern. It said it had taken Miss S's Universal Credit into account in the affordability assessment, but it didn't include her Disability Living Allowance.

It said it made a mistake when looking at Miss S's future first charge mortgage payments which may impact the affordability in the future, therefore it partially accepted the complaint. However, it said that although there was an oversight with the first charge mortgage, Miss S had withheld information from it about her gambling and reason for absence from work, which may have meant the mortgage may not have been approved. It offered £500 compensation for its error.

Miss S referred the complaint to the Financial Ombudsman Service where it was looked at by one of our Investigators. He said Pepper hadn't carried out adequate affordability and creditworthiness checks and had lent irresponsibly. He upheld the complaint.

Pepper didn't agree and so it was passed to me to decide.

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.

At the time of the lending decision, secured loan applications like this one were (and still are) covered by the rules of mortgage regulation, found in the MCOB section of the Financial Conduct Authority's Handbook.

The rules require a lender to assess affordability and not lend unless a loan is affordable. In making the assessment, a lender must obtain evidence of income, and information about expenditure. It can assess expenditure based either on a borrower's actual declared expenses, or it can use modelled expenditure information – such as typical expenditure figures for a household of this type – for living expenses but must always use actual figures for committed expenditure such as other credit agreements.

The rules also say that a lender is entitled to rely on what it's told about expenditure – unless, taking a common-sense view, it has reason to doubt it.

Miss S's credit file showed many active accounts, 6 of which had been taken out in the 12 months running up to this loan application, and 5 of those 6 being taken out just in April and June 2024.

Since April 2024 Miss S had taken out:

- In April 2024 a credit card with a £10,300 credit limit that had an outstanding balance of around £9,718
- In April 2024 a loan with a balance of around £12,300 and monthly payments of £293.
- In June 2024 a loan with a balance of around £15,000 and monthly payments of £393.
- In June 2024 a loan with a balance of around £13,440 and monthly payments of £224.
- In June 2024 a loan with a balance of around £12,690 and monthly payments of £264.

In addition, Miss S was also on a Mortgage Charter six-month interest only period with her first charge lender.

In the months leading up to taking out this secured loan, Miss S had taken on over £53,000 in unsecured debt and had needed to ask her mortgage lender for support with her first charge mortgage under the Mortgage Charter.

Pepper has said it asked about both, with Miss S saying the Mortgage Charter support was to save some money during the cost-of-living crisis, and the unsecured debt was to pay for a wedding (that was only in the planning stages such as booking a venue), a holiday and a car purchase.

Miss S's gross annual income from her employment at the time was around £43,000 so she had borrowed more than her gross annual salary in the three months from April to June 2024. Whilst paying for a wedding, a holiday and a car purchase may seem reasonable, it doesn't seem that Pepper asked questions about how that was split and whether any further money would need to be spent on the wedding (which seems likely bearing in mind it seems Miss S said it was only in the planning stages of booking a venue). It also doesn't seem to

have questioned the fact her fiancée didn't live with her, and what impact them moving in (assuming they would do so) after the wedding would have on her finances, bearing in mind she was in receipt of benefits that would be reviewed. It also doesn't seem from the information provided that Pepper asked about the ages of Miss S's children and when she would stop receiving benefits for them bearing in mind this loan was taken out over a 30 year term.

Miss S admitted she needed help due to the cost-of-living crisis with her first charge mortgage (hence applying for support under the Mortgage Charter), and she'd also taken on unsecured debt totalling more than her gross annual salary in just a three-month period shortly before taking out this secured loan – things that can be indicative of a person seeking debt options, which could mean they were in financial difficulties and/or a spiral of debt. Putting everything together I think the bigger picture shows a consumer that wasn't managing her finances well at the time.

I've taken into account what Pepper has said, and the information it received at the time, as well as what the rules of mortgage regulation say.

I do think that Pepper ought to have made further enquiries into Miss S's expenditure and credit worthiness at the time. Although the minimum standard required by the rules is only to obtain information about expenditure, there is an overarching obligation to act fairly and as a responsible lender.

It seems reasonable to take from Miss S's wider circumstances that she was struggling to manage her finances at the time of the application. In those circumstances, I think – acting responsibly – Pepper ought to have satisfied itself that this lending was affordable and sustainable by making more detailed enquiries into Miss S's expenditure rather than taking what it was told at face value.

I think there were grounds for doubting whether Miss S was really living within her means. I'm therefore satisfied that, acting responsibly, Pepper ought to have made further enquiries as it had reason to doubt what it had been told, and that should have included requesting copies of her bank statements.

I've reviewed the bank statements and I'm satisfied that, had Pepper viewed these at the time, then it shouldn't have lent because the loan would have been shown to have been unaffordable and irresponsible.

The bank statements show spending that was significantly higher than declared with substantial gambling transactions, payments being returned as unpaid, and payments not disclosed on the affordability assessment (such as additional payments for phone, TV and entertainment subscriptions, for example). The £15,000 loan went into Miss S's bank account on 19 June, and her bank statements show she had spent over £9,000 on gambling transactions on 21 and 22 June.

Whilst some of the additional spending could be discretionary expenditure, it still needs to be considered and a discussion held about which payments could possibly be reduced and to what level. But bearing in mind the level of gambling transactions, it doesn't seem Miss S was in a position – at that time – to reduce her spending to a level where this loan would have been affordable and sustainable. The bank statements we hold show that these transactions were not out of character – they reflect other transactions in the months before and after the loan application.

I don't think it's enough for Pepper to say it relied on what Miss S told it about her expenditure, and that she didn't declare any reasons why the loan might be problematic. It's

not enough to rely on what the applicant says alone when, as here, there were clear grounds, on a common-sense view, for doubting it.

For all the reasons given, I think the information Pepper used to assess Miss S's affordability significantly underestimated her expenditure, and based on the information that would have been available at the time (had it been asked for), it's more likely than not that the loan wasn't affordable and sustainable for Miss S, and that Pepper didn't take reasonable steps to ascertain whether it was or carry out a sufficiently robust affordability assessment.

Having considered everything very carefully I'm not persuaded Pepper acted responsibly when it agreed to lend to Miss S, and so I uphold this complaint.

Putting things right

To put matters right, Pepper should bring the loan agreement to an end and remove any adverse entries associated with this loan from Miss S's credit file.

Pepper sent £12,977.72 of the funds directly to Miss S. The volume of gambling transactions on Miss S's bank statements were extremely unlikely to be representative of someone who was gambling in a mindful or enjoyable way. After the money from the loan had been deposited into Miss S's account on 2 September it seems she had gambled all of it within a week or so.

Having reviewed the way Miss S had been managing her money in the months leading up to the loan application I think it was evident that there was a high risk she would use some or all of the funds to gamble – likely causing Miss S further harm and indebtedness.

As I think there was an obvious risk that Miss S would use the funds Pepper paid to her for gambling, rather than for home improvements, I think Pepper should write off that £12,977.72 of the capital as had that not been sent to Miss S then she couldn't have spent it on gambling.

It should also remove the £5,590 fees from the balance, as well as all interest charged on the borrowing to date. If any other fees have been added to the balance over the life of the loan those should also be removed. Pepper should then treat all the payments Miss S has made as payments reducing the capital balance. I understand Miss S is in the process of selling the property the loan is secured over. When that happens Pepper should waive any Early Repayment Charge and Mortgage Exit Administration Fee. This forms part of the removal of any fees, but I mention it here separately as I'm aware a sale is imminent and so it is clear to both sides what should happen.

Once the account has been reworked as I've set out above, this will result in a balance outstanding, so if the property sale doesn't complete, Pepper should reach a sustainable arrangement with Miss S for the repayment of the remaining outstanding capital balance, without applying future interest, and it can retain the charge over the property in the meantime.

I understand Pepper feels it shouldn't have to remove the broker fee as that wasn't money it received, but if it hadn't lent to Miss S then she wouldn't have incurred that broker fee, so the fact Miss S owes that sum on this loan is directly attributable to the lending decision made by Pepper. My role is to put Miss S back in the position she would have been in had this lending decision not been made, and that position is that she wouldn't owe that broker fee. It isn't relevant to my decision that Pepper didn't receive benefit from the fee.

I don't think it would be fair to ask Pepper to write off the remaining capital balance (other than the amount I've detailed above) or to refund the payments made towards that capital. Miss S used the remainder of the capital to pay off other debts, so it's fair and reasonable that she pays back what she borrowed. But it's not fair and reasonable for Miss S to pay fees and interest for a loan Pepper should not have entered into.

It is possible Miss S would have come to some arrangement with her unsecured creditors had this loan not existed. So it's not possible to be sure exactly what capital or interest Miss S would have had to pay if the debts had not been consolidated into this loan.

It's likely that removing all interest from this loan results in a saving to Miss S compared to the amount she would have had to pay towards the consolidated debts had they not been consolidated. But it's also possible she would have entered an arrangement such as an IVA or bankruptcy which would have led to her paying less (though with other consequences).

It's likely there is some saving in removing interest from the loan. But nevertheless I think it's a fair outcome to this complaint because I don't think it's fair and reasonable for Pepper to recover fees and interest charged under a loan agreement that ought never to have been entered into.

Although the existence of this loan caused Miss S distress and inconvenience, with the added worry that it was secured over her property, I don't propose to compensate Miss S separately for the distress and inconvenience this lending and the associated financial difficulties caused her so I don't award the £500 Pepper offered in its response to the complaint. I think the saving made in writing off the interest on this loan, compared to what she would likely have had to pay had the debts not been consolidated, represents fair compensation for that.

My final decision

For the reasons I've given, I uphold this complaint and direct UK Mortgage Lending Ltd trading as Pepper Money to put matters right in the way I've set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Miss S to accept or reject my decision before 5 January 2026.

Julia Meadows
Ombudsman