Financial Ombudsman Service

complaint

Mrs K complains that Studio Retail Limited ("Studio") lent to her in an irresponsible manner.

background

Mrs K was provided with a catalogue shopping account by Studio in October 2008. Her credit limit was initially set at £80 and was then increased almost monthly until it reached £726 in December 2009. There was a large increase in the credit limit to £1,286 in January 2010, with further increases in the following months before the limit reached £1,950 in November 2010.

The credit limit remained at that level for around a year before being reduced in April 2012. It started to rise again around four months later peaking at £1,576 in October 2012 before stabilising at £1,280 in March 2013. It remained around that level for the rest of the time Mrs K held the account. Around that time Studio had restricted Mrs K's use of the account and she wasn't allowed to make any new purchases.

Mrs K's account was defaulted in August 2017. Her outstanding balance was transferred to a third-party debt collection company. A balance remained outstanding when she brought her complaint to this Service.

Mrs K's complaint has been assessed by one of our adjudicators. He didn't think Studio's initial decision to open an account for Mrs K was unreasonable. And he hadn't seen any evidence to make him think the early credit limit increases hadn't been made responsibly. But he thought that by the time the credit limit was increased in November 2010 Studio should have realised that Mrs K was becoming reliant on this credit and so shouldn't have agreed that increase. And he thought that by January 2011 Studio should have reached the conclusion that Mrs K would be unable to repay what she'd borrowed in a sustainable manner. So Studio should have stopped offering further credit at that point and prevented Mrs K from making any new purchases using the account. So he asked Studio to put things right for Mrs K.

Studio let us know that it intended to complete a further investigation on the complaint. But since then it has failed to provide any further response to the assessment. So, as the complaint hasn't been resolved informally, it has been passed to me, an ombudsman, to decide. This is the last stage of our process. If Mrs K accepts my decision it is legally binding on both parties.

my findings

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint. We've set out our approach to unaffordable/irresponsible lending complaints on our website and I've kept this in mind while deciding Mrs K's complaint.

The regulations regarding lending of this type were evolving at the early stages of Mrs K's agreement with Studio. But certainly by 2010 the rules and regulations required Studio to carry out a reasonable and proportionate assessment of whether Mrs K could afford to repay what she owed in a sustainable manner. This assessment is sometimes referred to as an "affordability assessment" or "affordability check". The check needed to be completed at the outset of a relationship and each time there was a significant increase in the credit limit.

Studio also needed to monitor the account for any signs that Mrs K was struggling to manage the credit she'd been given.

The checks had to be "borrower" focused – so Studio had to think about whether repaying the credit sustainably would cause difficulties or adverse consequences for Mrs K. In practice this meant that Studio had to ensure that making the required repayments wouldn't cause Mrs K undue difficulty or adverse consequences. In other words, it wasn't enough for Studio to simply think about the likelihood of it getting its money back, it had to consider the impact of any repayments on Mrs K.

Checks also had to be "proportionate" to the specific circumstances at that time. In general, what constitutes a proportionate affordability check will be dependent upon a number of factors including – but not limited to – the particular circumstances of the consumer (e.g. their financial history, current situation and outlook, and any indications of vulnerability or financial difficulty) and the amount / type / cost of credit they are seeking.

In light of this, I think that a reasonable and proportionate check ought generally to have been *more* thorough:

- the *lower* a customer's income (reflecting that it could be more difficult to make any repayments to credit from a lower level of income);
- the *higher* the amount due to be repaid (reflecting that it could be more difficult to meet higher repayments from a particular level of income);
- the *longer* the period of time a borrower will be, or has been, indebted for (reflecting the fact that the total cost of the credit is likely to be greater and the customer is required to make repayments for an extended period).

There may also be other factors which could influence how detailed a proportionate check should've been for a given application – including (but not limited to) any indications of borrower vulnerability and any foreseeable changes in future circumstances. I've kept all of this in mind when thinking about whether Studio did what it needed to before agreeing to open an account for Mrs K, and to agree the subsequent increases to her credit limit.

Given the time that has elapsed since the account was first opened, Studio has told us that it has little evidence of the checks that it performed to ensure that Mrs K would be able to repay the credit in a sustainable manner. But it says that it would have used information from a credit reference agency to help determine the state of Mrs K's finances.

I don't draw any adverse conclusions from Studio's inability to provide me with the results of its checks. But without that information it would be difficult to fairly conclude that the checks it did were proportionate. It doesn't seem to have gathered any information from Mrs K about her specific circumstances.

But the credit limit it agreed when the account was first opened was relatively small - I don't think it would've been proportionate for Studio to ask Mrs K for the amount of information that would be needed to show the lending was unsustainable before opening the account. So I don't think the original lending decision should cause me any great concerns.

And I think the same applies to the increases to the credit limit that took place over the following two years, and particularly in the light of the relevant regulations only recently being finalised. During that time Mrs K appears to have operated her account relatively well, maintaining its balance within the agreed credit limit, and generally making the required repayments on time. Although I think Studio should have started to become increasingly concerned that Mrs K wasn't making any inroads into repaying what she owed, and her outstanding balance was steadily increasing, I don't think it unfair that Studio continued to offer, and increase, the credit to Mrs K.

Studio increased Mrs K's credit limit to £1,950 in November 2010. By then she had been borrowing for more than two years, and had made little progress in reducing her outstanding balance. In fact over the whole of that period there had only been a handful of occasions when Mrs K's balance had fallen month to month, and even then the reduction usually amounted to just a few pounds.

Studio was required to ensure that Mrs K would be able to repay what she owed over a reasonable period of time. So I would expect to see that Mrs K's balance was fluctuating with periods where she owed much less than the credit limit she had been granted. As I've explained above, that pattern was not shown by Mrs K's borrowing. So that didn't suggest that she would find it possible to repay what she owed in a sustainable manner over a reasonable period of time. Although it does seem that she was meeting the minimum repayments that the agreement required her to make, her debt appears to have been increasing unsustainably. So I don't think it was reasonable for Studio to increase the credit limit at that time.

I think there also comes a point where a lender needs to decide that simply maintaining a credit limit isn't enough. Where a consumer is making no progress in reducing their outstanding balance over a period of time it is generally a sign they are facing severe problems managing their finances. The availability of new credit needs to be withdrawn and a lender needs to show forbearance and stop adding interest to the account. That would mean that any payments made by the consumer would be used to reduce the outstanding balance rather than meet the purchase price of new goods or historic interest charges. Here, I agree with our adjudicator that point had been reached by January 2011.

By that time Mrs K had been borrowing from Studio for well over two years. She continued to show no evidence of her ability to repay what she owed. As soon as her credit limit had been increased in November she quickly spent more, and increased her outstanding balance back towards its maximum permitted level. I think that should have led to Studio curtailing the credit it was offering to Mrs K. I don't think it was appropriate for it to allow her to continue to make new purchases with the account, without a significant and sustained reduction in what she owed. In my view Studio's actions unfairly prolonged Mrs K's indebtedness by allowing her to use credit she couldn't afford and the interest being added got her into further debt.

So in summary, I don't think Studio should have increased the credit limit on Mrs K's account after, and including, the increase in November 2010. And I think it should have stopped adding interest to the account and letting Mrs K take any further credit from January 2011. So I uphold part of Mrs K's complaint and Studio needs to pay her some compensation.

putting things right

I don't think that Studio should have increased Mrs K's credit limit in, or after, November 2010. And I think Studio should have exercised forbearance and also not allowed Mrs K to make any further use of the credit facility after January 2011. So, to put things right, Studio should reconstruct Mrs K's account by making the following adjustments;

- rework the account to ensure that from November 2010 to Janaury 2011 interest is only charged on the first £1,623 outstanding to reflect the fact that no further credit limit increases should have been provided. The rework should then factor in that no interest at all should have been charged on the account from January 2011 onwards. All late payment and over limit fees should also be removed; and

- If an outstanding balance remains on the account once these adjustments have been made Studio should contact Mrs K to arrange a suitable repayment plan for this. If Studio considers it appropriate to record negative information on Mrs K's credit file, it should backdate this to November 2010.

OR

- If the effect of removing all interest, fees and charges results in there no longer being an outstanding balance, then any extra should be treated as overpayments and returned to Mrs K, along with 8% simple interest on the overpayments from the date they were made (if they were) until the date of settlement. If no outstanding balance remains after all adjustments have been made, then Studio should remove any adverse information from Mrs K's credit file.†

†HM Revenue & Customs requires Studio to take off tax from this interest. Studio must give Mrs K a certificate showing how much tax it's taken off if she asks for one.

From what I've seen, Studio sold the outstanding balance on this account to a third-party debt purchaser. So it either needs to buy the account back from the third party and make the necessary adjustments, pay an amount to the third party in order for it to make the necessary adjustments, or pay Mrs K an amount to ensure that it fully complies with this direction.

my final decision

My final decision is that I uphold part of Mrs K's complaint and direct Studio Retail Limited to put things right as detailed above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs K to accept or reject my decision before 19 April 2021.

Paul Reilly
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