Financial Ombudsman Service

complaint

Mr T has complained about short term loans given to him by Instant Cash Loans Limited (trading as "The Money Shop"). He's said he shouldn't have been given these loans as they were unaffordable to him.

background

Mr T took four loans in total with The Money Shop. His borrowing history is as follows:

- Loan one taken in December 2010 for £200 – Mr T deferred paying this loan on two occasions
- Loan two taken in April 2011 for £250
- Loan three taken in July 2011 for £250 – Mr T deferred paying this loan on one occasion
- Loan four taken in October 2011 for £250 - Mr T paid a number of late fees as a result of being unable to repay this loan on time.

One of our case handlers looked at what The Money Shop and Mr T said. He thought that The Money Shop's checks before agreeing to any of these loans weren't proportionate. He also thought that proportionate checks wouldn't have made a difference to loans one and two but that they would most likely have shown The Money Shop it shouldn't have given loans three and four to Mr T.

Mr T didn't disagree with our adjudicator's view. But The Money Shop didn't accept it. So the case has been passed to an ombudsman for review. As neither Mr T or The Money Shop have disagreed with our adjudicator's view on loans one and two, this decision is only looking at whether loans three and four should have been given to Mr T.

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 explained how we handle complaints about short term lending on our website. And I've used this approach to help me decide Mr T's complaint.

Having carefully thought about everything I've been provided with, I'm upholding Mr T's complaint. I'd like to explain why in a little more detail.

the relevant regulatory considerations and guidance in place at the time of the loans

I've seen what The Money Shop has said about assessing this complaint under Financial Conduct Authority ("FCA") principles. Given it has talked about fairness, I'm assuming that it is referring to Principle six, which requires an authorised firm to pay due regard to the interests of its customers and treat them fairly.

The first thing for me to say is that the FCA Principles of for Business ("PRIN") set out the overarching requirements that businesses are required to comply with. But the principles do not replace the relevant regulatory obligations that are in place in a relevant business sector. And this means that a regulated business is required to adhere to the principles as well as (rather than instead of) any regulatory obligations in place in its relevant sector.

In any event, I'd also point out that The Money Shop gave Mr T these loans during the period it held a standard licence from the Office of Fair Trading ("OFT"), which enabled it to carry out consumer credit activities. So while I think that businesses should always look to treat customers fairly, The Money Shop wasn't even regulated by the FCA at the time it gave Mr T these loans. And at the time the OFT had clear guidance in place which lenders were expected to follow when deciding to lend money.

I've seen the arguments The Money Shop has made about Mr T's loans being cheque based and so arguably outside the scope of normal lending decisions. I'm also aware of the Bill of Exchange Act 1882. I accept that The Money Shop may have had greater confidence that it would receive payment because it already had a cheque from Mr T. But The Money Shop entered into agreements for credit that were regulated by the Consumer Credit Act 1974, with Mr T.

So it was clearly providing credit to Mr T otherwise there would've been no need to get him to sign a regulated agreement. And as a result I'm satisfied that the Money Shop was making a lending decisions which were in effect covered by the then regulator of Consumer Credit Licensees the OFT as I haven't seen any exception for cheque based loans.

Indeed it could also be argued that the product was designed and offered in the way it was precisely because The Money Shop had concerns that it would receive payment from a borrower. After all why would it insist on a number of cheques for the maximum amount guaranteed by the consumer's cheque guarantee card (thus guaranteeing it would receive the whole amount of what it lent) rather than a single cheque covering the whole amount of a loan, if it was confident it would receive payment in full and on time. Surely this would have been far easier from an administrative point of view.

The OFT issued guidance ("ILG"), in March 2010, which it said represented its view on irresponsible lending. Given when Mr T's loans were taken, I consider this to have contained the relevant regulatory obligations that The Money Shop should have had in mind when deciding whether to lend to Mr T.

The ILG specifically states *"Assessing affordability' is a borrower-focussed test which involves a creditor assessing a borrower's ability to undertake a specific credit commitment, or specific additional credit commitment, in a sustainable manner, without the borrower incurring (further) financial difficulties."* The guidance goes on say that repaying credit in a sustainable manner means being able to repay credit *"out of income and/or available savings."*

It then goes onto to say *"The purpose of payday loans is to act as a short-term solution to temporary cash flow problems experienced by consumers. They are not appropriate for supporting sustained borrowing over longer periods, for which other products are likely to be more suitable."* And finally it says that *"The creditor should take a view on what is appropriate in any particular circumstance dependent on, for example, the type and amount of the credit being sought and the potential risks to the borrower."*

In practice all of this meant that a lender had to take proportionate steps to ensure a consumer would've been able to repay what they were borrowing in a sustainable manner without it adversely impacting on their financial situation. Put simply the lender had to gather enough information so that it could make an informed decision on the lending.

Although the guidance itself didn't set out compulsory checks, it did list a number of things a lender could take into account before agreeing to lend. The key thing was that the rules required a lender's checks to be proportionate. And any checks had to take into account a number of different things, such as how much was being lent and when what was being borrowed was due to be repaid.

Having reviewed The Money Shop's arguments, I also want to make it clear that I don't think it would ever be correct for a lender to advance credit to a consumer, without carrying out some sort of proportionate borrower focused assessment, simply because they may end up repaying less than twice the amount they borrowed.

Just because the amount of interest paid may be less than the cap introduced by the FCA - in January 2015 – this in itself doesn't mean that a loan is affordable. As far as I'm concerned, the total cost of the credit and the duration of the agreement are merely factors to think about when considering what sort of information is needed for any checks on affordability to be proportionate.

I've kept all of the above in mind when thinking about whether The Money Shop did what it needed to before agreeing to these loans. It's my understanding that Mr T was given loans where there was an expectation, at least at the outset, that the capital borrowed plus the interest due was to be repaid in a single payment. So overall I think this means The Money Shop's checks had to provide enough for it to be able to understand whether Mr T would be able to make these payments when they fell due.

It looks like Mr T provided a payslip confirming his income. It also looks as though Mr T selected an option confirming that his gross monthly creditor commitments were somewhere between £300 and £499. I can also see that The Money Shop retained a portion of a bank statement. I presume it took this from Mr T in order to verify his identity and to confirm his salary was being paid into the account his cheques were issued from.

why I don't think The Money Shop checks were proportionate

I've thought about what The Money Shop has provided and what it has said. But overall given what The Money Shop knew about Mr T, I think it would've been proportionate to carry out further checks before it agreed to give these loans

To explain, The Money Shop would've been aware that Mr T was on a relatively low income and that the amount he had to repay for loans three and four took up a significant proportion of his monthly income. And the portion of Mr T's bank statement that The Money Shop had also showed a significant amount of gambling transactions as well as returned direct debits.

Given the proportion of Mr T's income that was going towards these loans and the total amount of the gambling transactions and Mr T's returned direct debits, I think that The Money Shop needed to find out more about Mr T before lending to him. This is especially as this was Mr T's third loan within a short period of time and his two deferrals of his first one suggests that there might have been a possibility Mr T had difficulty repaying it.

In these circumstances, I think that The Money Shop should've done more to investigate Mr T's actual financial position. So overall having carefully thought about everything, I think that The Money Shop failed to carry out proportionate checks before agreeing to give loans three and four to Mr T.

what I think proportionate checks would most likely have shown

Even though I don't think the checks The Money Shop carried out were proportionate, this doesn't, on its own, mean Mr T's complaint should be upheld. After all if further checks would've simply shown The Money Shop that Mr T would most likely have been able to make the payments he was committing to when they became due (and so there was no reason why The Money Shop shouldn't have lent to Mr T), then further checks wouldn't have made a difference. This is because Mr T won't have lost out because of The Money Shop' failure to carry out proportionate checks and there'd be no reason for me to uphold the complaint.

But if further checks would most likely have shown Mr T was unlikely to have been able to make these payments then The Money Shop would've seen that it shouldn't have lent to him. And this would mean that Mr T lost out because of The Money Shop' failure to carry out proportionate checks. So there'd be grounds to uphold Mr T's complaint.

As proportionate checks weren't carried out I can't know what exactly they would have shown. But Mr T has provided us with evidence of his financial circumstances at the time he asked for these loans. And I've been able to get a picture of what his financial circumstances were like.

Of course I accept this isn't perfect as different checks show different things. And just because something shows up in the information Mr T has provided it doesn't mean it would've shown up in any extra checks The Money Shop might've carried out. But what Mr T has provided is the best indication I have of his financial circumstances at the time of the applications. And in the absence of anything else I think it's perfectly reasonable to rely on it.

I've carefully looked through everything Mr T's provided and I've also thought about everything both parties have said. Having done so, I don't think Mr T had the capacity to take on these loans. As explained, based on what The Money Shop had seen, I think that proportionate checks would've extended into finding out about more about Mr T expenditure and verifying this.

I think if such checks had been carried out at the correct time they would've shown that Mr T didn't really have enough to be able to sustainably repay these loans once his normal monthly living costs and his payments to existing creditors were deducted from his salary.

I also think that proportionate checks would have shown The Money Shop that Mr T was borrowing from other short term lenders to support his income. And when these commitments are added to his existing ones, the amount he had to pay out each month was more than what he earnt. And this doesn't even take into account the amount Mr T was gambling either.

So I think that if The Money Shop had taken a proportionate look into Mr T's circumstances by further investigating the questions posed by the information it had, it would've seen that Mr T was unlikely to have been able to repay these loans sustainably and without it adversely affecting his financial position. And it follows that I don't think The Money Shop would've given these loans if it had carried out proportionate checks.

Overall I think not only did The Money Shop fail to carry out proportionate checks before giving loans three and four to Mr T, but that Mr T also lost out as a result of this.

what The Money Shop should do to put things right

To put things right for Mr T, The Money Shop should:

- refund all the interest and charges applied on loans three and four; and
- add interest at 8% per year simple on the above interest and charges from the date they were paid to the date of settlement †;
- remove any adverse information recorded on Mr T's credit file as a result of these loans;

†HM Revenue & Customs requires The Money Shop to take off tax from this interest. The Money Shop must give Mr T a certificate showing how much tax it's taken off if he asks for one.

my final decision

For the reasons given above, I uphold Mr T's complaint. Instant Cash Loans Limited (trading as The Money Shop) should pay Mr T compensation as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr T to accept or reject my decision before 2 March 2018.

Jeshen Narayanan
ombudsman