Financial Ombudsman Service

complaint

Mr H complains that NewDay Ltd, trading as Aqua, ("NDL"), was irresponsible when it agreed to open a credit card account for him and when it later increased his credit limit on two occasions. Mr H says the credit was unaffordable for him.

background

Mr H opened a credit card account with NDL on 21 February 2014. NDL gave him a £250 credit limit to start with. But it then increased the credit limit to £550 in August 2014 and again increased it to £1,300 in July 2015. The account went into arrears and the debt was sold to a third party, ("T"), in July 2016.

Mr H said that NDL should never have allowed him to open an account. When he applied, NDL should have checked his credit record. It would have seen he had recent missed payments to his overdraft, and a default for this only just before. His overdraft had been increasing for several months in a row.

In addition, Mr H said that NDL should never have increased his credit limit. He had only made minimum payments for a long while and he was using a very high level of his credit limit. This should have shown NDL that he couldn't repay his balance within a reasonable length of time. So, NDL shouldn't have let him borrow more. If the lender had properly checked Mr H's credit record before increasing the credit limit, it would have seen that in the two years since his account had been opened, additional late payment markers and defaults had been put on his credit file and he'd taken out a lot of other credit. This should have warned NDL that he was struggling with his finances and it was not responsible for it to lend him more. By increasing Mr H's credit limit, NDL made his financial position worse. In 2014, his monthly take home pay was £1,000 but his monthly expenses were £1,200 and his monthly debt repayments were over £100. The minimum repayments to NDL were over £100. Mr H couldn't afford his existing debt and he was having to borrow more every month.

In its final response letter, NDL said it had considered the information Mr H supplied on his credit application and the information held at the Credit Reference Agencies ("CRAs"). Mr H said he had an annual income of £16,000. He also had one defaulted account, but this occurred 37 months prior to his application. NDL said that Mr H met its acceptance criteria and as a result, he was provided with its card and a credit limit of £250.

NDL said that it regularly reviewed how Mr H was using the card, along with how he was managing his other credit commitments. It said that this type of review might result in either an increase or decrease to the credit limit. In August 2014, Mr H's account was reviewed, and his credit limit was increased from £250 to £550. This increase was offered in a letter dated 20 August 2014 and Mr H was provided with an opportunity to 'opt out' of the increase. But it had no record of Mr H contacting it to 'opt out' of the credit limit increase. A further review took place in July 2015 and the credit limit was increased from £550 to £1,300. It again had no record of Mr H contacting it to 'opt out' of the credit limit increase.

Our adjudicator's view

Our adjudicator noted that at account opening NDL had completed a credit check and asked Mr H about his income. She said it was reasonable for NDL to have relied on the information Mr H provided at the time. She appreciated NDL's credit check showed that Mr H had one default but given the proposed credit limit was a minimal amount and there was nothing else concerning on the credit file, she didn't think NDL needed to do anything more.

The adjudicator had then reviewed Mr H's account management before the first credit limit increase. She could see that he'd exceeded his credit limit on several occasions and felt this raised concerns about his financial situation which should've prompted NDL to have completed a more detailed review of Mr H's financial circumstances. She'd reviewed Mr H's bank statements and concluded that it wasn't sustainable to lend to Mr H.

The adjudicator noted that Mr H continually exceeded his credit limit before the second credit limit increase. She thought this showed he was struggling financially. She'd again reviewed Mr H's bank statements and concluded that it wasn't sustainable for NDL to lend. The adjudicator said that by approving this credit limit, NDL was increasing Mr H's indebtedness to NDL, and his overall indebtedness. She recommended that NDL pay Mr H some compensation and remove any negative information from Mr H's credit file from the time of the first credit limit increase.

NDL disagreed with the adjudicator's recommendations. It said that at the point of the first credit limit increase, there were no financial difficulty or affordability indicators reported to it by the CRA it used. Additionally, the CRA reported a low overall indebtedness and so NDL didn't think it had any reason to believe that an increase of £300 to a total credit limit of £550 would not be sustainable. NDL said that it often started with a low credit limit and reviewed the account with a view to increasing at regular intervals. Whilst overlimit fees were incurred early on, NDL didn't think this was indicative of Mr H not being able to manage the account, but more that when he first used the account, the total transactions meant he had exceeded the given limit by £14.95 by his first statement. This then had a knock-on effect until he paid the balance in full in May 2014. NDL didn't believe that there were any financial difficulty signals at this point and Mr H had paid the account in full.

But NDL could see that after the first credit limit increase, the risk data had changed. The number of active accounts shown by the CRA increased as had Mr H's overall indebtedness. It also started to see the worst status field in the credit file change. NDL said that it now thought that the second credit limit increase was not appropriate, and it was willing to refund all interest and charges applied after the second increase. This would be offset against any balance outstanding with T.

The adjudicator asked NDL if it would also remove any associated adverse information on Mr H's credit file.

NDL responded to say that it didn't agree to amend Mr H's credit file, as it was obliged to provide a true reflection of Mr H's payment history. It calculated at that time that a total refund of £212.09 would be offset against Mr H's outstanding balance.

Mr H said that he wouldn't accept NDL's offer as he wanted the adverse information to be removed from his credit file and for the outstanding balance to be cleared.

my provisional decision

After considering all the evidence, I issued a provisional decision on this complaint to Mr H and to NDL on 12 February 2021. I summarise my findings:

As NDL had agreed that the second credit limit increase wasn't appropriate, I said that I didn't intend to investigate this but would include the redress for it in my redress section.

I noted that the Office of Fair Trading ("OFT") was the regulator when Mr H applied for the credit card. The Financial Conduct Authority ("FCA") was the regulator when NDL increased the credit limits on the account. The relevant rules and guidance set out by the OFT and the FCA were similar, with the FCA rules and guidance referencing what went before. The rules and guidance of both regulators obliged NDL to lend responsibly and were respectively contained in the OFT's Irresponsible Lending Guidance ("ILG") and the FCA's Consumer Credit Sourcebook ("CONC").

Guidance issued by the OFT in early 2008 explained that its aim was to ensure that an appropriate standard of consumer protection was in place, telling lenders that "the way you operate any aspect of a business might well be relevant to your fitness to hold a consumer credit licence."

Irresponsible lending was included in this guidance as an example of an unfair or improper practice, and defined as being "contrary to the provisions of section 25(2B) of the Consumer Credit Act 1974, by failing to take reasonable care in making loans or advancing lines of credit, including making only limited or no enquiries about consumers' income before offering loans, and failing to take full account of the interests of consumers in doing so."

In early 2010 the OFT published the ILG. Paragraph 4.2 of the ILG stated:

Whatever means and sources of information creditors employ as part of an assessment of affordability should be sufficient to make an assessment of the risk of the credit sought being unsustainable for the borrower in question. In our view this is likely to involve more than solely assessing the likelihood of the borrower being able to repay the credit in question.

Paragraph 4.3 stated: The OFT regards 'in a sustainable manner' in this context as meaning credit that can be repaid by the borrower: • without undue difficulty – in particular without incurring or increasing problem indebtedness • over the life of the credit agreement or, in the case of open-end agreements, within a reasonable period of time • out of income and/or available savings, without having to realise security or assets.

This meant that NDL needed to check that Mr H could afford to meet his repayments in a sustainable manner, in other words being able to meet his repayments out of his normal income without having to go without or borrow further.

The ILG and CONC weren't prescriptive about what checks NDL needed to carry out in order to reasonably assess whether or not Mr H would be able to meet his repayments sustainably. But the regulations said that such checks needed to be proportionate. This suggested that the same checks might not be the appropriate thing to do for all consumers, or for the same consumer in all circumstances.

In general, I would expect a lender to require more assurance the greater the potential risk to the consumer of not being able to repay the credit in a sustainable way. So, for example, I would expect a lender to seek more assurance by carrying out more detailed checks. These factors include:

- the lower a customer's income (reflecting that it could be more difficult to make any credit repayments from a lower level of income);

- the higher the amount due to be repaid (reflecting that it could be more difficult to meet a higher repayment from a particular level of income);
- the longer the period of time during which a customer had been given credit (reflecting the risk that repeated refinancing might signal that the borrowing had become, or was becoming, unsustainable).

There might even come a point where the lending history and pattern of lending itself clearly demonstrated that the lending was unsustainable.

In the case of credit cards, a lender needed to assess whether a borrower could afford to repay the credit within a reasonable period of time. What constituted a reasonable period of time wasn’t defined but the ILG suggested *“the borrower should be able to repay the credit on a timeline at least akin to that used for other forms of unsecured lending such as fixed sum personal loans, made for an amount equivalent to the credit limit.”*

With regard to assessing a credit limit, the box under Section 4.6 of the ILG said *“ We consider that the credit limit should have been set by the creditor (presumably aware of the borrower's current disposable income and any reasonably foreseeable future changes in the level of his disposable income - for example, if the borrower is close to retirement age and facing a significant fall in disposable income) on the basis of having undertaken an appropriate affordability assessment.”*

CONC also required a lender to undertake an assessment of the consumer’s creditworthiness before significantly increasing the credit limit for a credit card.
CONC 5.3.1G said that:

(9) For a regulated credit agreement for running-account credit the firm should set the credit limit based on the creditworthiness assessment or the assessment required by CONC 5.2.2R (1) and taking into account the matters in CONC 5.2.3 G, and, in particular, the information it had on the customer's current disposable income taking into account any reasonably foreseeable future changes.

Bearing all of this in mind, I’d considered the following questions:

- did NDL complete reasonable and proportionate checks when assessing Mr H’s credit application and credit limits to satisfy itself that he would be able to repay the credit in a sustainable way?

- if not, what would reasonable and proportionate checks have shown?

- did NDL make fair lending decisions?

<u>Did NDL complete reasonable and proportionate checks?</u>

Account application

I’d noted that NDL had carried out a credit check before Mr H opened his account. NDL had seen a defaulted account on its check which occurred more than three years before his application. This didn’t appear to have given it concerns.

We hadn’t received a credit report from Mr H which showed his credit commitments at the time of his application for the credit card and at the time of the first credit limit increase. So, I couldn't say that there were any entries on this that might have given NDL additional concerns.

But I thought that NDL also needed to consider Mr H's monthly net income and regular expenditure, including his other regular credit commitments to reasonably assess whether Mr H could manage to meet repayments on his credit card account. As shown above, the ILG presumed this information would be gathered by a lender when setting a credit limit. I'd noted that Mr H had declared an annual income of £16,000 and I could see that NDL's application data showed he had an unsecured credit balance of £1,700. But I couldn't see that it had obtained any other information about his expenditure. So, I couldn't see that NDL had carried out a proportionate check when Mr H applied for the credit card.

Credit limit increase on 28 August 2014

As I'd said above, CONC specifically mentioned taking into account a customer's disposable income when setting a credit limit.

NDL told us:-

"When making a decision to increase a credit limit we would consider things such as utilisation, account maintenance as well as Bureau data and our own internal risk strategies. At the time of the increases Mr [H] had passed the Affordability and Financial Difficulties checks that we are required to complete. We also checked for Over Indebtedness, Credit Utilisation, Arrears, CCJ's and Defaults using bureau information, of which also passed the criteria. Late payments will not affect a credit limit increase offer, as long as the customer does not allow the account to become delinquent and pays before the next statement is issued. The same applies when a customer exceeds the credit limit. In the instance that a customer exceeds the credit limit, as long as appropriate action is taken within the statement month to bring the account back in order, this will not affect the increase. Only if the account remains over its limit or delinquent at the time the increase is due to take effect will the offer be withdrawn."

I hadn't seen any information gathered by NDL before the credit limit increase other than what it had told us in its response to the adjudicator's view and information about how Mr H had managed his card repayments in its risk data.

The credit checks carried out by NDL appeared to provide no concerns.

In addition, NDL didn't think the overlimit fees Mr H incurred early on were indicative of him not being able to manage the account.

I'd reviewed NDL's risk data which showed Mr H's spending and payments on the card account. I could see that Mr H had spent around £247 in the month after account opening. I could see that £140 was spent on cash withdrawals which could be a sign of financial difficulties. So, after his first month, Mr H was already very near his credit limit. It then appeared that Mr H didn't make any payments to the account in April 2014. He then repaid his full statement balance in May 2014. He then paid £5 towards a balance of £247.55 in June 2014. It was difficult to tell from the account terms received from NDL if this was the minimum payment at the time or less than the minimum payment. Mr H's account again exceeded the credit limit in July 2014, but this appeared to be mainly because an overlimit fee was incurred. And Mr H had increased his monthly repayment to £38.01 in July 2014.

I'd noted that NDL's account terms say the credit limit is the total amount a borrower can borrow from NDL at any one time and that a borrower's balance must never be more than their credit limit. But I could see that Mr H's account balance had exceeded the credit limit for four of the six months prior to the first credit limit increase. And in the month of the credit limit increase, the account balance was only around £4 below the credit limit.

Overall, despite the full balance being repaid in May 2014, I couldn't see that Mr H was acting in line with the account terms for most of his time as an account holder before the credit limit increase. So, I didn't think the credit limit should have been increased without NDL carrying out more checks. And I thought that it would have been proportionate for NDL to have obtained information about Mr H's then disposable income and any short term financial commitments in view of his borrowing history with it.

We hadn't received any other evidence from NDL to show that it obtained any information from Mr H about his income, regular expenditure and short term financial commitments at the time of the first credit limit increase. Nor could I see that we'd received any information from NDL about a credit check around the time of the increase. The most recent credit check information appeared to be from April 2014 which showed that Mr H had three credit cards with a balance of £221.

So overall, I didn't think that NDL had carried out a proportionate check on Mr H's ability to repay his credit in a sustainable manner when it increased his credit limit in August 2014, notwithstanding that the lender said it had considered bureau data and checked for affordability and financial difficulties.

But the failure to carry out a proportionate check in itself didn't mean that Mr H's complaint should succeed. I also needed to be persuaded that what I considered to be proportionate checks would have shown NDL that Mr H couldn't sustainably afford the credit. So, I'd looked at Mr H's bank statements to see what better checks would have shown NDL.

What would reasonable and proportionate checks have shown and did NDL make fair lending decisions?

Account opening

As I'd said above, I would have expected NDL to obtain information about Mr H's regular expenditure before lending and I couldn't see that it had done that. Mr H had provided some bank statements from around the time he'd applied for the credit card. I wasn't suggesting that this was the check that NDL should have done. But I thought looking at his bank statements gave me the best picture of what the lender should have seen.

I'd reviewed Mr H's bank statements for the month before he'd opened the account to see what better checks would have shown about Mr H's expenses. Although Mr H told us in his complaint form that he was spending £1,200 on regular expenses and £100 on debt repayments, I could see very little expenditure on living costs on the bank statements we'd received. But I could see that Mr H had two other bank accounts from the transfer information on his statements. So, I'd asked the adjudicator to ask Mr H for the statements for these accounts to see if these showed other spending on living costs. We'd received the statements for one of the accounts which was another current account. The other account was a savings account. Having reviewed the statements for the second current account, I couldn't see specific expenditure on living costs.

Mr H said that when he opened the account, there were recent missed payments to his overdraft, and a default for this only just before. Mr H said that his overdraft had been increasing for several months in a row. I'd seen bank statements for Mr H's main current account from 2 January 2014, but his account hadn't been overdrawn from that date to the date he'd taken out the credit card. I could see on the second current account that a payment for around £39 had been returned in mid-January 2014 and had then been represented a week later when there were no funds in the account and had been returned again. But overall, I didn't think this would have given NDL additional concerns.

Overall, I wasn't persuaded that better checks would reasonably have led NDL to conclude that it shouldn't have lent to Mr H. I didn't think the bank statements showed any obvious evidence that Mr H was facing problems managing his finances and that the credit limit of £250 would be unsustainable for Mr H. And I didn't think his finances would have appeared under so much pressure that NDL should have declined his application.

Credit limit increase August 2014

It seemed to me that NDL didn't properly consider Mr H's wider financial circumstances when increasing his credit limit, despite explaining that its assessment took into account various checks.

As I'd said above, I would have expected NDL to obtain information about Mr H's income, regular expenditure and short term lending before increasing his credit limit and I couldn't see that it did that.

I'd reviewed Mr H's bank statements (including the second current account statement) for several months before the first credit limit increase to understand what his income, living costs and credit commitments were around that time. I'd also taken into account Mr H's spending patterns to get a better picture of Mr H's financial situation. I'm not suggesting here that these are the checks that NDL should have done. But I thought looking at his bank statements gave me the best picture of Mr H's wider circumstances which the lender would have likely seen if it had made better checks.

I could see that Mr H's living costs had increased substantially since he'd taken out the card and his expenditure on his credit commitments was around the same level as when he'd taken out the card. I could also see that Mr H needed to take out a short term loan each month to supplement his income. I thought the regular spending and borrowing patterns shown on Mr H's bank statements would likely have caused NDL some concerns had it made better checks before increasing the credit limit. In Mr H's circumstances I thought there was a significant risk that Mr H wouldn't have been able to repay a balance around the amount of the new credit limit within a reasonable period of time without having to go without or without borrowing further. So, I wasn't persuaded that NDL had acted fairly in increasing Mr H's credit limit at this point.

So, I intended to say that NDL could have done more before providing the credit card and before increasing the credit limit in August 2014. And if it had made better checks, it was likely to have found that Mr H's circumstances at the time of the first credit limit increase had suggested that the additional credit wasn't likely to be sustainable. So, I wasn't persuaded that NDL had acted responsibly at that time. Subject to any further representations by Mr H or NDL my provisional decision was that I intended to uphold this complaint in part. I intended to order NDL to put things right as follows.

What NDL should do to put things right

NDL has already agreed that it shouldn't have increased Mr H's credit limit a second time. NDL has agreed to refund all interest and charges applied after the second credit limit increase. It said that this would be offset against the balance outstanding with the debt agent (should there still be one), but if Mr H has since paid the balance then the refund would go directly to him. But it didn't agree to remove adverse information on his credit file.

Where we find credit to have been agreed irresponsibly, this Service's approach to putting things right includes the removal of adverse information on the consumer's credit file as the credit shouldn't have been lent. I see no reason why the adverse entries on Mr H's credit file arising from the second credit limit increase shouldn't be removed here once any amount owed has been settled.

In order to put things right for him NDL should:

a) remove all interest and charges on the account arising from transactions made on or after the date of the first credit limit increase ("CL1 date"); and
b) add the capital cost of any transactions made after the CL1 date to the outstanding balance Mr H owed prior to the CL1 date;
c) treat any payments Mr H had made since the CL1 date as payments towards the balance calculated in a) + b).
d) If this clears the balance any funds remaining should be refunded to Mr H along with 8% simple interest* calculated from the date of these overpayments to the date of settlement or if an outstanding balance remains, NDL needs to treat Mr H sympathetically and fairly, which may mean agreeing an affordable repayment plan with him; and
e) remove any negative information about the account from the CL1 date onwards from Mr H's credit file once any amount owed has been settled.

As the debt has been sold to a third party ("T") NDL should either repurchase it and ensure the above steps are carried out or liaise with T to bring these about

* HM Revenue & Customs requires NDL to take off tax from this interest. NDL must give Mr H a certificate showing how much tax it has taken off if he asks for one. If NDL intends to use the refunds to reduce an amount Mr H owes, it must do this after tax.

Mr H responded to my provisional decision to say that he agreed it. He wanted confirmation that the default and charges would be removed.

NDL responded to my provisional decision to say it was happy to settle the case in line with my provisional decision. It confirmed that it would ask T to update Mr H's credit file and remove the default.

my findings

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

I note that Mr H was seeking confirmation that the default and charges would be removed. I note that NDL has confirmed that it will ask T to remove the default from Mr H's credit file. And as I've said above in my redress section, I've ordered NDL to remove all interest and charges on the account arising from transactions made on or after the date of the first credit limit increase and to remove any negative information about the account from the CL1 date onwards from Mr H's credit file once any amount owed has been settled.

Otherwise, given that Mr H and NDL have given me nothing further to consider, I see no reason to depart from the conclusions I reached in my provisional decision. It follows that I uphold part of the complaint and require NDL to take the steps and pay Mr H some compensation as set out below.

my final decision

My decision is that I uphold this complaint in part. In full and final settlement of this complaint I order NewDay Ltd, trading as Aqua, to:

a) remove all interest and charges on the account arising from transactions made on or after the date of the first credit limit increase ("CL1 date"); and
b) add the capital cost of any transactions made after the CL1 date to the outstanding balance Mr H owed prior to the CL1 date;
c) treat any payments Mr H had made since the CL1 date as payments towards the balance calculated in a) + b).
d) If this clears the balance any funds remaining should be refunded to Mr H along with 8% simple interest* calculated from the date of these overpayments to the date of settlement or if an outstanding balance remains, NDL needs to treat Mr H sympathetically and fairly, which may mean agreeing an affordable repayment plan with him; and
e) remove any negative information about the account from the CL1 date onwards from Mr H's credit file once any amount owed has been settled.

As the debt has been sold to a third party ("T") NDL should either repurchase it and ensure the above steps are carried out or liaise with T to bring these about

* HM Revenue & Customs requires NDL to take off tax from this interest. NDL must give Mr H a certificate showing how much tax it has taken off if he asks for one. If NDL intends to use the refunds to reduce an amount Mr H owes, it must do this after tax.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr H to accept or reject my decision before 8 April 2021.

Roslyn Rawson
ombudsman