

## Complaint

Mr S has complained that London Mutual Credit Union Limited (LMCU) did not carry out proper affordability checks before providing him with loans. Mr S says that, had further checks been carried out by LMCU, it would've seen that he was borrowing from a number of different pay day lenders.

## Background

LMCU provided Mr S with lending between March 2014 and March 2015. Based on information provided to this service, a summary of Mr S's lending history can be found below:

loan number	loan amount	received date	actual repayment date
1	£400.00	27/03/2014	10/06/2014
2	£1,500.00	29/05/2014	09/03/2015
3	£400.00	11/06/2014	28/07/2014
4	£500.00	29/07/2014	01/09/2014
4a	£400.00	02/09/2014	26/09/2014
4b	£500.00	29/09/2014	01/11/2014
4c	£400.00	03/11/2014	02/12/2014
4d	£500.00	03/12/2014	29/12/2014
4e	£400.00	05/01/2015	03/02/2015

Mr S complained to LMCU who provided him with a final response letter, explaining that it didn't think it had made an error by providing the above lending. Unhappy with this response Mr S brought his complaint to our service.

One of our adjudicators looked at what LMCU and Mr S said. She thought that LMCU hadn't done anything wrong when it provided these loans.

LMCU accepted what the adjudicator concluded and didn't have any additional comments.

Mr S disagreed with our adjudicator's assessment. In response he made a number of comments including:

- had LMCU reviewed his credit file at the time it would've seen he was heavily in debt;
- Mr S had lending with other short-term loan providers at the time; and
- Mr S became dependent on these loans.

As no agreement could be reached the case has been passed to me, an ombudsman, for a decision.

## My findings

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

To start with it may help if I outline the regulatory framework that was applicable at the time LMCU provided these loans to Mr S. This is important, because what was required of LMCU before it lent to Mr S plays a key part in deciding whether it did something wrong.

As a credit union, I think it's fair to say that LMCU is looked at and treated slightly differently from other lenders by the industry regulator, the Financial Conduct Authority ("FCA").

This can be seen in a speech given to Credit Unions in January 2020 called, *"Is this the decade of the Credit Union?"* Below I've included some extracts of that speech, that I think are useful in understanding the FCA's long term thinking around the role that credit unions can play in the consumer credit market.

***"The need***

*We enter the 2020s with large numbers of people in the United Kingdom having very low financial resilience, as a result of high debt, low savings or both.*

*By reducing the volume of unaffordable credit being granted by the commercial consumer credit sector, we are improving consumer outcomes. And at the same time, we're levelling the playing field a little, so that credit unions have a better chance of engaging with consumers before they fall into the hands of lenders with a very different set of values.*

***Conclusion***

*As we start the new decade, we have an opportunity to discuss the vision for the sector which credit unions would like to realise by 2030, and to be clear about the roles that credit unions, government, regulators and others would need to play for that vision to become reality.<sup>1</sup>*

The FCA's thinking around the use of credit unions, and why they are different, is further demonstrated in the November 2018 FCA policy paper (CP18/35) called, *"Rent-to-own and alternatives to high-cost credit"* following its review of that sector of the market. In that paper, the FCA said, *"We have also looked at alternatives to high-cost credit, recognising that not all consumers will have access to mainstream credit, and that lower-cost and non-credit options may exist"*. The FCA suggested this policy paper may be of relevance to credit unions.

The purpose of the review is described in this way:

*"2.4 RTO (Rent-to-Own) is just one part of our high-cost credit review. We are developing proposals for consultation and finalising measures that we consulted on in May 2018. These include measures on overdrafts, home-collected credit, catalogue and store cards and buy now pay later deals."*

And the FCA has suggested credit unions are a viable alternative to the types of credit provider outlined in 2.4:

*"4.45 Credit unions and community development financial institutions (CDFI) will be a viable alternative for some. However, these have traditionally been small scale and/or limited to particular geographic areas."*

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<sup>1</sup> <https://www.fca.org.uk/news/speeches/decade-credit-union>

The paper then goes on to explain the following:

*“6.10 While there may be alternatives to high-cost credit for these customer groups, there are barriers to their access. In summary, these are:*

- limited availability of alternatives (supply side)*
- limited consumer awareness of alternatives (demand side) “*

And:

*“6.17 At present, the main providers of alternative, lower cost credit for higher risk consumers are credit unions”*

This paper also briefly touches on the legislation that caps the interest rate for lending, meaning anything below that cap is what we call ‘exempt’.

*“6.19 For the protection of their members, legislation sets a lending interest rate cap for credit unions. Lending is capped at 3% per month (approximately 42.6% APR) in England, Wales and Scotland, and at 1% (around 12.9% APR) in Northern Ireland. This makes credit union loans cheaper alternatives to high-cost credit. While some of the larger credit unions have broadened their lending bases to include higher risk consumers, others do not feel able to do so within the cap, or do not wish to for business reasons”*

The agreements Mr S took out with LMCU were what are called “exempt” agreements. This means that they fell outside many of the rules and requirements that other lenders (such as ‘payday’ or longer-term lenders) needed to follow, because the LMCU lending was at a lower rate of interest, below the “cap” talked about above. I’ve had to keep this in mind when deciding whether or not it’s fair and reasonable in this case to say that LMCU did (or didn’t) do anything wrong.

When loan one was approved, LMCU was overseen by the Office of Fair Trading (OFT). From loan two, it was a regulated firm, meaning it came under FCA regulation for consumer credit from 1 April 2014.

The FCA’s Principles for Business (*PRIN*) set out the overarching requirements which all authorised firms are required to comply with. And the Credit Union sourcebook (*CREDs*) 10.1.3 confirms *“The Principles (PRIN) apply to all credit unions”*. So in this context, I consider it reasonable to take into account what PRIN says.

The Principles themselves are set out in PRIN 2.1.1R. And the most relevant principle here is PRIN 2.1.1 R (6) which says:

*“A firm must pay due regard to the interests of its customers and treat them fairly.”*

PRIN is applicable to all FCA regulated lenders. So, I must consider LMCU’s overarching responsibility to treat Mr S fairly.

As I’ve explained, these loans are “exempt” agreements. That said, the credit union trade body – the Association of British Credit Union Limited (ABCUL), of which LMCU is a member – explained in a response to FCA consultation paper CP13/10 (which detailed proposals for FCA regulation of consumer credit industry):

*“Ahead of its officially inheriting oversight of consumer credit regulation from April 2014, the Financial Conduct Authority is running a high-profile consultation which looks at the detailed regulatory framework which it proposes to adopt. While much of this will only affect credit unions indirectly given the exemption of credit union loans from consumer credit regulation, it is still important that credit unions are aware of the regulations others in the industry are required to comply with....<sup>2</sup>”*

Although the above press release reaffirms that LMCU are exempt from some of the consumer credit regulations, the response to the consultation does suggest that LMCU needed to be aware of the regulations that other consumer credit lenders and providers of non-exempt agreements needed to adhere to. And these wider industry regulations can be found in the Consumer Credit sourcebook (CONC) section 5, which outlines a firm’s obligation in relation to responsible lending.

In addition, following the FCA’s review of high cost credit creditworthiness assessments outlined in CONC, ABCUL said:

*“The FCA also published a new consultation on clarified rules and guidance in relation to creditworthiness and affordability assessments. While most credit union lending is exempt from these requirements, they should always be looked to as best practice and we will be summarising and circulating details of these proposals in due course. The consultation focuses particularly on the distinction between credit risk and affordability, the use of income and expenditure information and considerations for lenders in making their assessments proportionate.<sup>3</sup>”*

So, LMCU is a regulated firm and its own industry trade body has said it is good industry practice to be mindful of the wider rules and regulations that other consumer credit providers are required to abide by. That seems fair and reasonable to me.

Indeed, when considering Mr S’s case I’m required to consider all the available evidence and arguments to decide what’s fair and reasonable in the circumstances. As such, I think it’s right to take into account the wider industry regulations at the time, which can be found in CONC 5 and 6. After all, I’m required to consider good industry practice – amongst other things – when reaching my decision in this case.

As I’ve mentioned, CONC 5 and CONC 6 were introduced in April 2014. As is evident from the following extracts, the FCA’s CONC rules specifically note and refer back to sections of the OFT’s *Irresponsible Lending Guidance* on many occasions. (That was the OFT guidance that the consumer credit industry was expected to follow up to the point the FCA took over regulation in April 2014.)

Section 5.2.1R(2) of CONC sets out what a lender needs to do before agreeing to give a consumer a loan of this type. It says a firm must consider:

- (a) *“the potential for the commitments under the regulated credit agreement to adversely impact the customer’s financial situation, taking into account the information of which the firm is aware at the time the regulated credit agreement is to be made; and*

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<sup>2</sup> <https://www.abc.ul.coop/viewdocument/financial-conduct-authority-cp-13-1>

<sup>3</sup> <https://www.abc.ul.coop/blogs/patrick-thorpe/2019/01/28/fca-publishes-review-of-high-cost-credit>

*[Note: paragraph 4.1 of ILG]*

*(b) the ability of the customer to make repayments as they fall due over the life of the regulated credit agreement, or for such an agreement which is an open-end agreement, to make repayments within a reasonable period.*

*[Note: paragraph 4.3 of ILG]*

CONC also includes guidance about 'proportionality of assessments'. CONC 5.2.4G(2) says:

*"A firm should consider what is appropriate in any particular circumstances dependent on, for example, the type and amount of credit being sought and the potential risks to the customer. The risk of credit not being sustainable directly relates to the amount of credit granted and the total charge for credit relative to the customer's financial situation."*

*[Note: paragraph 4.11 and part of 4.16 of ILG]*

CONC 5.3 contains further guidance on what a lender should bear in mind when thinking about affordability. And CONC 5.3.1G(1) says:

*"In making the creditworthiness assessment or the assessment required by CONC 5.2.2R (1), a firm should take into account more than assessing the customer's ability to repay the credit."*

*[Note: paragraph 4.2 of ILG]*

CONC 5.3.1G(2) then says:

*"The creditworthiness assessment and the assessment required by CONC 5.2.2R (1) should include the firm taking reasonable steps to assess the customer's ability to meet repayments under a regulated credit agreement in a sustainable manner without the customer incurring financial difficulties or experiencing significant adverse consequences."*

*[Note: paragraph 4.1 (box) and 4.2 of ILG]*

#### Section 140 of the Consumer Credit Act 1974

All of Mr S's loans were given to him after Section 140 of the Consumer Credit Act came into force on 6 April 2007. Section 140A sets out circumstances where the court may determine that the relationship between a creditor and a debtor is unfair to the debtor. Section 140A says:

##### **"140A Unfair relationships between creditors and debtors**

*(1) The court may make an order under section 140B in connection with a credit agreement if it determines that the relationship between the creditor and the debtor arising out of the agreement (or the agreement taken with any related agreement) is unfair to the debtor because of one or more of the following-*

- (a) *any of the terms of the agreement or of any related agreement;*
  - (b) *the way in which the creditor has exercised or enforced any of his rights under the agreement or any related agreement;*
  - (c) *any other thing done (or not done) by, or on behalf of, the creditor (either before or after the making of the agreement or any related agreement).*
- (2) *In deciding whether to make a determination under this section the court shall have regard to all matters it thinks relevant (including matters relating to the creditor and matters relating to the debtor).*
- (3) *For the purposes of this section the court shall (except to the extent that it is not appropriate to do so) treat anything done (or not done) by, or on behalf of, or in relation to, an associate or a former associate of the creditor as if done (or not done) by, or on behalf of, or in relation to, the creditor.*
- (4) *A determination may be made under this section in relation to a relationship notwithstanding that the relationship may have ended.*
- (5) *An order under section 140B shall not be made in connection with a credit agreement which is an exempt agreement [for the purposes of Chapter 14A of Part 2 of the Regulated Activities Order by virtue of article 60C(2) of that Order (regulated mortgage contracts and regulated home purchase plans)]”*

Section 140B sets out the types of order the court could make should it determine that the relationship between the creditor and debtor is unfair to the debtor:

***“140B Powers of court in relation to unfair relationships***

- (1) *An order under this section in connection with a credit agreement may do one or more of the following—*
  - (a) *require the creditor, or any associate or former associate of his, to repay (in whole or in part) any sum paid by the debtor or by a surety by virtue of the agreement or any related agreement (whether paid to the creditor, the associate or the former associate or to any other person);]*
  - (b) *require the creditor, or any associate or former associate of his, to do or not to do (or to cease doing) anything specified in the order in connection with the agreement or any related agreement;*
  - (c) *reduce or discharge any sum payable by the debtor or by a surety by virtue of the agreement or any related agreement;*
  - (d) *direct the return to a surety of any property provided by him for the purposes of a security;*
  - (e) *otherwise set aside (in whole or in part) any duty imposed on the debtor or on a surety by virtue of the agreement or any related agreement;*
  - (f) *alter the terms of the agreement or of any related agreement;*
  - (g) *direct accounts to be taken, or (in Scotland) an accounting to be made, between any persons.”*

In respect of the need to double-check information disclosed by applicants, CONC 5.3.1G(4) has a reference to paragraphs 4.13, 4.14, and 4.15 of the ILG and states:

*(a) "it is not generally sufficient for a firm to rely solely for its assessment of the customer's income and expenditure on a statement of those matters made by the customer."*

And CONC 5.3.7R says that:

*"A firm must not accept an application for credit under a regulated credit agreement where the firm knows or ought reasonably to suspect that the customer has not been truthful in completing the application in relation to information supplied by the customer relevant to the creditworthiness assessment or the assessment required by CONC 5.2.2R (1)."*

**[Note: paragraph 4.31 of ILG]**

From a regulatory perspective, there are exemptions from CONC for certain types of loans – which, as I've explained, are the same loans which were provided to Mr S by LMUC. But it is clear, in the wider industry publications, that CONC is at least considered best practice. And in terms of treating customers fairly, which LMCU was required to do as a regulated lender, I'm going to keep this in mind.

### **The complaint**

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

Firstly, it seems that Mr S was provided with a number of different products by LMCU:

- loans 1 and 3 were 'payday' loans with repayments to be made over three monthly instalments;
- loan 2 was a longer-term consolidation loan, to be repaid over 12 months (payments of £134 per month). But importantly, the balance was secured on shares that Mr S had with LMCU; and
- loan 4 was a revolving 'payday' loan – where Mr S could draw up to his credit limit (in this case £500).

I've kept all of this in mind when thinking about the checks that LMCU carried out.

LMCU called some of the loans 'payday loans' but these loans were not high cost short term credit loans (HCSTC) in the traditional sense as defined by the FCA. The FCA defines HCSTC as fulfilling the following criteria:

- a borrower – lender agreement
- the APR is equal to or exceeds 100%
- the credit should be substantially repaid within a maximum of 12 months from the date the credit is given.<sup>4</sup>

The loans provided to Mr S were due to be repaid within a number of months. However, they don't fall under the above definition because the APR for each loan was around 42.6%. This is important, because it is well below the threshold outlined above. So, it is clear the loans provided by LMCU are not HCSTC lending as defined by the FCA.

<sup>4</sup> <https://www.handbook.fca.org.uk/handbook/glossary/G3328.html>

When thinking about what, if anything, LMCU has done wrong, I've kept in mind all the wider industry regulation I've listed above, and what LMCU says about these loans. And I've distilled my thinking into the following questions:

- Did LMCU complete reasonable checks to satisfy itself that Mr S would be able to repay his loans in a sustainable way?
  - If so, did it make a fair lending decision?
  - If not, would those checks have shown that Mr S would've been able to do so?
- Bearing in mind the circumstances, at the time of each application, was there a point where LMCU ought reasonably to have realised it was increasing Mr S's indebtedness in a way that was harmful and / or unfair so shouldn't have provided further loans?
- Did LMCU act unfairly or unreasonably in some other way?

If I determine that LMCU didn't act fairly and reasonably in its dealings with Mr S, and that he has lost out as a result, I will go on to consider whether compensation is due.

*Did LMCU complete reasonable checks to satisfy itself that Mr S would be able to repay the loans in a sustainable way?*

Good industry practice at the time for LMCU ought to have led it to carry out a reasonable assessment as to whether Mr S could afford to repay the loans in a sustainable manner.

The industry guidance at the time, as I've mentioned above, spoke about "*borrower*" focused assessment. So LMCU needed to think about whether repaying the loan sustainably would cause difficulties or adverse consequences for Mr S.

LMCU also needed to think about what a reasonable check would be, in the circumstances of each application. And the guidance at the time suggested that a number of factors needed to be considered, such as Mr S's financial history, current situation and outlook, any indications of vulnerability or financial difficulty and the amount of credit he was asking for.

Effectively, this means that the information LMCU may have needed to have gathered before approving each loan would evolve over time, depending on what it knew about Mr S.

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

- the *lower* a customer's income (reflecting that it could be more difficult to make any loan repayments to a given loan amount 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 term of the loan (reflecting the fact that the total cost of the credit is likely to be greater and the customer is required to make payments for an extended period); and
- the *greater* the number and frequency of loans, and the longer the period of time during which a customer has been given loans (reflecting the risk that repeated



refinancing may signal that the borrowing had become, or was becoming, unsustainable).

Were LMCU's checks reasonable?

When thinking about whether LMCU carried out reasonable checks, I've kept in mind that Mr S was provided with a number of different products, the products were exempt agreements, and the fact that Mr S borrowed from a credit union and not either a mainstream lender or a high cost credit provider.

From what I've seen, for each loan LMCU appears to have asked Mr S to declare his income and LMCU has shown that it took on at least one occasion a copy of Mr S's payslip as well as letter from his employer. So, I'm satisfied that LMCU had a fairly accurate idea of his actual income from at least loan two.

LMCU also appeared to have asked Mr S some fairly detailed information about his living costs such as mortgage, utility bills and other loans. And, based on what LMCU gathered, it would've appeared to it that Mr S would've been able to afford the loan repayments that he was committed to repaying.

LMCU also appears to have carried out credit scoring exercises before approving some of the loans and indeed this appeared to be the main way it approved the payday loans it provided to Mr S. Given the amounts borrowed, I don't consider this to be an unreasonable check.

For loan two it looks like LMCU was provided with an overview from a well-known credit reference agency – which I believe Mr S provided. And having looked at this overview, there wasn't anything in it to suggest to LMCU that Mr S was either having financial difficulties or was dependent on other forms of lending (such as pay-day lending).

However, LMCU was aware of two defaults. One recorded in 2013 and one at the start of 2014. But there wasn't anything else in the checks that would've alerted LMCU to wider problems, and given the dates of the defaults, I don't think this ought to, in itself, have led LMCU to decline the applications or ask Mr S for further information.

Before loan two was granted LMCU gathered copies of Mr S's bank statements. I've considered these statements because if a review of them suggested Mr S wouldn't be able to afford to repay the loan, then LMCU ought not have provided it.

Having looked at the statements, there is some other borrowing, but there is no indication from what I've seen that Mr S couldn't afford the repayments to LMCU, even factoring those other existing repayments in. So, based on what LMCU would've seen on the bank statements, it would've likely concluded – and reasonably so – that the loans were affordable.

There also isn't any other indication, such as how Mr S repaid the earlier loans, to have led LMCU to believe that it needed to carry out further or more detailed checks as its lending relationship with him progressed. Indeed, the information gathered by LMCU indicated that he would be in a position to repay these loans.

I accept that Mr S's full circumstances may not have been entirely reflected in the information he provided, or the other information LMCU obtained. And Mr S's actual financial

position might well have been apparent if further information – such as bank statements or a full credit check – had been taken at other points in the lending relationship.

But, overall, I think the checks that LMCU carried out before it provided these loans went far enough. The checks that it did do demonstrated to it that Mr S would be in a position to repay these loans. So, I don't think it was wrong of LMCU to have given Mr S his lending.

Bearing in mind the circumstances, at the time of each application, was there a point where LMCU ought reasonably to have realised it was increasing Mr S's indebtedness in a way that was harmful and / or unfair so shouldn't have provided further loans?

This is a further consideration because in addition to assessing the circumstances behind each *individual* loan provided to Mr S by LMCU, I also think it's fair and reasonable to look at the *overall pattern* of lending and what unfolded during the course of Mr S's lending relationship with LMCU.

I'm mindful here that wider industry rules and guidance – as summarised in the earlier part of this decision – make it clear that a lender shouldn't continue lending where the loans are unsustainable or otherwise harmful and/or it's apparent that the customer may be experiencing financial difficulties. And it seems to me that there may come a point at which a responsible lender ought fairly and reasonably to question whether continuing to offer further lending to a customer who appears to be persistently and repeatedly reliant upon borrowing was unsustainable or otherwise harmful. And I've carefully considered whether that point was reached in this case.

But, looking at the individual circumstances of this case, I don't think either the number of loans, or the time that Mr S had been indebted to LMCU, should've led it to conclude that Mr S had become reliant and/or dependent on this lending.

Did LMCU act unfairly or unreasonably towards Mr S in some other way?

I've carefully thought about everything provided. Having done so, I've not seen anything so far that leads me to conclude that LMCU acted unfairly or unreasonably towards Mr S in some other way.

## **conclusions**

Overall, and having carefully thought about the three overarching questions set out above, I've seen nothing that would lead me to conclude that LMCU acted unfairly or unreasonably when it provided these loans to Mr S. I appreciate Mr S will be disappointed with the outcome but I want to assure him that I have considered all the evidence that has been provided.

## **My final decision**

For the reasons I've explained, I'm not upholding Mr S's complaint, and I make no award against London Mutual Credit Union Limited.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr S to accept or reject my decision before 18 January 2021.

Robert Walker  
**Ombudsman**