

complaint

Mr S has complained about an instalment loan he took out with Madison CF UK Limited (trading as “118 118 Money”) in 2017. Amongst other things, he’s said that the loan was unaffordable and so 118 118 Money lent to him irresponsibly.

background

Mr S initially complained about having been provided with two instalment loans by 118 118 Money. The first loan was provided in October 2016. It was for £2000 and due to be repaid in 24 instalments. This loan was settled when Mr S applied for further borrowing in November 2017. The November 2017 loan was for £2779.24 (which included an amount of £1529.24 to clear the outstanding balance on the October 2016 loan – so Mr S received £1250.00) and this loan was also due to be repaid over 24 months.

When it initially investigated Mr S’ complaint, 118 118 Money accepted that it shouldn’t have provided the October 2016 loan. It refunded the interest Mr S paid and then reduced the balance on the November 2017 loan to reflect the fact that Mr S borrowed extra in order to repay his first loan. Mr S was dissatisfied at 118 118 Money’s response as he thought that it was unfair for it to have provided his November 2017 loan too.

One of our adjudicators looked at what 118 118 Money and Mr S said. He thought that 118 118 Money unfairly provided the November 2017 loan to Mr S. So our adjudicator thought that Mr S’ complaint should be upheld. As 118 118 Money disagreed with our adjudicator, the complaint has been passed to me for a final decision.

As 118 118 Money has already agreed that it shouldn’t have provided the October 2016 loan to Mr S, this decision isn’t looking at whether it acted unfairly at this time. All I’m looking at is whether 118 118 Money acted fairly and reasonably in providing the November 2017 loan to Mr S and what effect this has on what it has already agreed to do to put things right for the October 2016 loan.

the regulatory framework

118 118 Money was authorised and regulated by the Financial Conduct Authority (“FCA”) when it lent to Mr S. The relevant rules and regulations FCA regulated firms are required to follow are set out in the FCA’s Handbook of rules and guidance.

- *the FCA Principles for Business (“PRIN”)*

The FCA’s Principles for Business set out the overarching requirements which all authorised firms are required to comply with.

PRIN 1.1.1G, says

The Principles apply in whole or in part to every firm.

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.

- *the Consumer Credit sourcebook ("CONC")*

This sets out the rules which apply to providers of consumer credit like 118 118 Money. CONC also replaced the requirements set out in Section 55B CONC 5 sets out a firm's obligations in relation to responsible lending. And CONC 6 sets out a firm's obligations after a consumer has entered into a regulated agreement.

It's clear there is a high degree of alignment between the Office of Fair Trading's ("OFT") Irresponsible Lending Guidance ("ILG") and the rules set out in CONC 5 and CONC 6. 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.

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*

[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.

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]

CONC 5.3.1G(6) goes on to say:

For the purposes of CONC "sustainable" means the repayments under the regulated credit agreement can be made by the customer:

- (a) without undue difficulties, in particular:
 - (i) the customer should be able to make repayments on time, while meeting other reasonable commitments; and*
 - (ii) without having to borrow to meet the repayments;**
- (b) over the life of the agreement, or for such an agreement which is an open-end agreement, within a reasonable period; and*
- (c) out of income and savings without having to realise security or assets; and*

"unsustainable" has the opposite meaning.

[Note: paragraph 4.3 and 4.4 of ILG]

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 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]

my findings

I have read and considered all the evidence and arguments available to me from the outset, in order to decide what is, in my opinion, fair and reasonable in all the circumstances of the case.

Taking into account the relevant rules, guidance, good industry practice and law, I think there are two overarching questions I need to consider in order to decide what's fair and reasonable in the circumstances of this complaint. These questions are:

- Did 118 118 Money complete reasonable and proportionate checks to satisfy itself that Mr S would be able to repay his loan 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?
- Did 118 118 Money act unfairly or unreasonably in some other way?

If I determine that 118 118 Money 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 what is fair compensation.

Did 118 118 Money complete reasonable and proportionate checks to satisfy itself that Mr S would be able to repay his loan in a sustainable way?

The rules and regulations in place at the time 118 118 Money lent to Mr S required it to carry out a reasonable and proportionate assessment of whether Mr S could afford to repay his loan in a sustainable manner. This is sometimes referred to as an "affordability assessment" or "affordability check".

The affordability checks had to be "borrower-focused" – so 118 118 Money had to think about whether Mr S would be able to repay the loan sustainably. In practice this meant that 118 118 Money had to ensure that making the payments to the loan wouldn't cause Mr S undue difficulty or adverse consequences. In other words, it wasn't enough for 118 118 Money to simply think about the likelihood of it getting its money back, it had to consider the impact of loan repayments on Mr S.

Any checks also had to be "proportionate" to the specific circumstances of the loan application. 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 borrower (e.g. their financial history, current situation and outlook, and any indications of vulnerability or financial difficulty) and the amount, type and cost of credit they are seeking. Even for the same customer, a proportionate check could look different for different loan applications.

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 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).

There may also be other factors which could influence how detailed a proportionate check should be for a given loan application – including (but not limited to) any indications of borrower vulnerability and any foreseeable changes in future circumstances. I've thought about all the relevant factors in this case.

Were 118 118 Money's checks reasonable and proportionate?

118 118 Money says it carried out a number of credit and affordability checks before it decided to lend to Mr S. It says that it carried out a credit check and its decision to lend was based on this, the income and expenditure information provided by Mr S and the bank statements requested. As far as 118 118 Money is concerned the loan was affordable based on everything it had.

I've carefully thought about what 118 118 Money has said. But it isn't enough just to carry out checks. A lender also needs to react to the information it receives. And, in this case, I'm mindful that Mr S was asked to provide copies of his most recent bank statements. The bank statements Mr S provided showed that Mr S had been taken out a significant number of high-cost short-term loans in the months leading up to the November 2017 application. Equally 118 118 Money appears to have been aware of the fact that Mr S had at least 13 loans of this type in the months leading up to November 2017.

118 118 Money says having existing short-term credit commitments didn't make Mr S ineligible for his loan. Mr S was asked what the purpose of this loan was and he said that he was going to use the funds to consolidate debts.

Indeed this loan was flagged as a payday rescue loan and Mr S' existing short-term lending commitments weren't considered because it was reasonable to assume that he would've used the funds obtained to settle the most expensive credit he had – the short-term loans on his credit file.

It says:

"Payday rescue is all about helping customers get better value credit on the basis that they would cease to need payday loans, hence we would expect to see this sort of behaviour - our experience shows that such customers are less likely to default on loans than average – perhaps because the repayments to us are less than they have become used to with payday loans companies."

I've carefully thought about what 118 118 Money has said. But I have to say that I have grave concerns with this approach for a number of reasons.

Firstly, 118 118 Money didn't actually take any steps to establish which debts, if any, Mr S would actually be consolidating with this loan. So while the purpose of this loan was recorded as debt consolidation, without knowing which, if any, debts Mr S would be consolidating, 118 118 always ran the risk that no existing debts would be cleared and this loan would simply increase Mr S' overall indebtedness. And by failing to take account of

which existing debts would be consolidated, I have to question how accurate any affordability assessment going forward would be.

Secondly 118 118 Money's comments about its experience showing that payday loan customers are less likely to default on loans appears to suggest that its only concern was whether it was likely to receive loan payments from a customer. As I've explained earlier, the rules, regulations and guidance in place all make it clear that a lender is required to do more than simply assess its own credit risk. It also needs to consider the impact of any lending on the customer.

In my experience, payday loan customers are indeed more likely to somehow make their loan repayments. But they often do so by unsustainably increasing their overall indebtedness by borrowing from a number of different sources including the lender concerned. So 118 118 Money relying on its experience of payday loan customers being more likely to make their payments and less likely to default as a factor in deciding whether to provide a loan, doesn't inspire confidence in the robustness of its borrower focused affordability assessment.

My final reason for concern here is that 118 118 Money appear to have disregarded the existing high-cost short term credit commitments that it was aware Mr S had. It has said that it didn't take Mr S' existing high-cost short term credit commitments into account because it was reasonable to assume that he'd used the funds being advanced to settle these loans. It assumed this would be the case because Mr S' high-cost short term loans were the most expensive credit Mr S had.

The first thing for me to say is that there isn't anything to suggest that Mr S intended to consolidate his existing short term lending commitments with this loan. 118 118 Money may have flagged the November 2017 loan as a 'payday rescue' loan. But I don't think that it and any reason to believe that the funds would be used for this specific purpose such as a declaration from Mr S that this was going to be the case. And for the reasons I've explained above, this means that 118 118 Money ran the risk of increasing Mr S' high-cost credit indebtedness by leaving him having to make payments to this loan as well as his existing ones.

I'd also point out that I would've had concerns with 118 118 Money's overall argument even if I were to accept its points on why it disregarded Mr S' existing high-cost short term credit commitments. Firstly, the amount of money it provided to Mr S for the November 2017 loan wasn't enough to clear all of Mr S' existing high-cost short term credit commitments. So I can't see how it could possibly have concluded that all of them would be settled.

Secondly, I also have significant concerns with the idea that Mr S using the funds from 118 118 Money to repay his existing high-cost short term credit commitments, somehow meant that he was being provided with better value credit. I say this because CONC5A.3.2 limits the total amount a borrower has to repay a high-cost short term credit provider to no more than twice the amount they initially borrowed.

So if I were to accept 118 118 Money's argument about the purpose of this loan, it will have effectively transitioned Mr S from a product where the total amount he could pay (including late payment and default fees) was capped to twice the amount initially borrowed, to a product where the amount he had to pay was uncapped. My own estimate indicates that Mr S had to pay around 1.5 times the amount of money received for the November 2017 loan in interest (when the interest on the amount advanced to settle the October 2016 loan is

excluded). And even then he didn't have enough funds to be able to clear all of his existing high-cost short term credit commitments.

Given the interest rate 118 118 Money charged on this loan and half of the total amount of credit was due to be repaid halfway into the term, there is an argument for saying that the November 2017 loan 118 118 Money provided Mr S was itself high-cost short term credit. And it should be subject to the cap in CONC5A.3.2 as a result.

I suspect that 118 118 Money's argument against this isn't that the credit it provided isn't high-cost but that it isn't short-term. And, in these circumstances, if I accept that the November 2017 loan was to be used to repay Mr S' high-cost short term credit commitments, 118 118 Money will have transitioned Mr S from high-cost short term credit to high-cost medium or long term credit. So given the total amount Mr S was required to pay on the November 2017 loan and the circumstances, I'm simply not persuaded by the argument that this loan represented better value credit than what 118 118 Money was assuming would be repaid.

Indeed I'd even go as far as saying that it is arguable that providing this type of credit in these particular circumstances for this particular purpose is, in itself, unlikely to be fair. But this isn't a matter for me to decide here, as I'm required to decide what's fair and reasonable in the circumstances of this case – not whether it would ever be fair for a lender to transition a customer from a loan where the total amount they could repay is capped to one which isn't and potentially could cost them substantially more.

And I don't think deciding this issue is crucial to me deciding what's fair and reasonable in the circumstances of Mr S' particular case. I say this because the information 118 118 Money obtained ought fairly and reasonably have alerted it to the fact that Mr S was unlikely to be able to sustainably make his repayments - irrespective of whether he intended to use the funds to repay his existing high-cost short term credit commitments.

As I've previously explained, CONC 5.3.1(2) G requires a lender to take reasonable steps to establish that a borrower will be able to sustainably make any repayments required by a credit agreement. CONC defines sustainable as without undue difficulties and in particular the customer should be able to make repayments on time, while meeting other reasonable commitments; as well as without having to borrow to meet the repayments.

So it follows that if a lender realises, or it ought fairly and reasonably to realise, that a borrower won't be able to make their repayments sustainably if they're unlikely to be able to make their repayments without borrowing further. And I think that the information 118 118 Money gathered ought fairly and reasonably to have alerted it to the fact that this is always what was likely to happen here.

To explain, 118 118 Money says the information it gathered suggested that Mr S was required to pay £1000 to unsecured loans and credit cards and that he was overdrawn by almost £5000. 118 118 Money will also have been aware of Mr S' monthly salary.

So 118 118 Money ought to have been aware that Mr S was unlikely to have reached a credit balance on his current account even if a whole month's salary was added to the money he received for the November 2017 loan. This doesn't even take into account the payments due on the unsecured loans and credit cards, Mr S' existing high-cost credit commitments and any other reasonable normal monthly living expenses.

As this was the case the information 118 118 Money obtained suggested that Mr S was always likely to remain substantially overdrawn during the period he was required to make repayments to this loan. Given just how overdrawn Mr S was likely to remain, 118 118 Money ought fairly and reasonably to have realised that Mr S was unlikely to be able to make his loan repayments while meeting other reasonable commitments and without having to borrowing further. And I think that the information 118 118 Money obtained ought fairly and reasonably to have alerted it to the fact that Mr S would not be able to sustainably make the repayments to the loan he was given in November 2017.

So having carefully considered everything I've seen on this case, I think 118 118 Money failed to proportionally react to the information it was provided with. This led to it unfairly and unreasonably providing Mr S with a loan he couldn't have sustainably repaid. And so 118 118 Money unfairly and unreasonably provided Mr S with an unsustainable loan.

Did 118 118 Money act unfairly or unreasonably in some other way?

I've carefully thought about everything provided. Having done so, other than by providing the loan, I've not seen anything here that leads me to conclude 118 118 Money acted unfairly or unreasonably towards Mr S in some other way.

Overall and having carefully thought about the two overarching questions, set out on page four of this decision, I think that 118 118 Money unfairly and unreasonably provided Mr S with a loan it ought to have realised he was unlikely to have been able to sustainably make the payments to. So 118 118 Money shouldn't have provided the November 2017 loan to Mr S.

As Mr S ended up paying interest and charges on a loan he couldn't reasonably have been expected to sustainably repay, I think that he lost out because of what 118 118 Money did wrong. So 118 118 Money should put things right.

fair compensation – what 118 118 Money needs to do to put things right for Mr S

I've carefully thought about what amounts to fair compensation in this case.

Where I find that a business has done something wrong, I'd normally expect that business – in so far as is reasonably practicable – to put the consumer in the position they *would be in now* if that wrong hadn't taken place. In essence, in this case, this would mean 118 118 Money putting Mr S in the position he'd now be in if he hadn't been given a loan in November 2017.

But when it comes to complaints about irresponsible lending this isn't straightforward. Mr S was given the loan in question and he's used the funds. So, in these circumstances, I can't undo what's already been done. And it's simply not possible to put Mr S back in the position he would be in if he hadn't been given these loans in the first place.

As this is the case, I have to think about some other way of putting things right in a fair and reasonable way bearing in mind all the circumstances of the case. And I'd like to fully explain the reasons why I think that it would be fair and reasonable for 118 118 Money to put things right in the following way.

interest and charges on the loans Mr S shouldn't have been given

As I've explained, 118 118 Money ought to have realised that it was providing Mr S with a loan that he was unlikely to be able to substantially repay. And in reality it's the interest that Mr S had to pay 118 118 Money on the November 2017 loan that is the problem, as he kept having to find additional funds (usually through borrowing elsewhere) to pay the interest on his 118 118 Money loan.

I'm also mindful that 118 118 Money has already attempted to put things right for the October 2016 loan which it accepts shouldn't have been provided to Mr S. So I think that the fairest way to ensure that Mr S is refunded any interest and charges that he may have paid on the November 2017 loan is to add the total amount of money he received as a result of being provided both of his loans (in other words £3200). 118 118 Money should then deduct any payments Mr S made from this amount. 118 118 Money should treat any payments made after the payments Mr S made reach a total of £3200 as overpayments. And to start with, I think that 118 118 Money should refund these overpayments as they will represent the interest Mr S paid as a result of being given his loans.

I've also given thought to the argument that Mr S had to borrow – from elsewhere – in order to repay the interest and charges he paid to 118 118 Money and so he should be refunded any borrowing costs he incurred to pay 118 118 Money's interest and charges.

I accept that there were occasions where Mr S was simply cycling money around borrowing from multiple sources in order to pay debts. For example, it's clear that Mr S made a number of payments by using his overdraft. And, in circumstances, where it is clear that a consumer incurred additional costs in order to be able to repay a lender's interest and charges, it might be appropriate to direct a lender to pay the consumer extra compensation to cover those additional costs.

But, in this case, Mr S was borrowing from so many different sources. And I can't see a clear correlation showing that funds from a particular source (or sources) of credit directly went towards repaying 118 118 Money's interest and charges. In other words, I can't say exactly what directly additional cost Mr S incurred at a given time. So, in these circumstances, I don't think that 118 118 Money should refund extra interest because Mr S might've paid interest elsewhere in order to repay his 118 118 Money loans.

That said, it's clear that Mr S did lose the use of the funds he used to pay the interest, I now think that 118 118 Money needs to refund to him. As Mr S lost the use of these funds, I think that he should be compensated for this.

We normally ask a business to pay 8% simple interest where a consumer hasn't had the use of funds because its actions resulted in something having gone wrong. Bearing in mind my conclusions in the paragraph above, I see no reason to depart from our usual approach here and I think awarding 8% per year simple interest, on the interest and charges that were paid (in other words any overpayments over and above the amount of money Mr S received), is fair and reasonable in the circumstances of this case.

Mr S' credit file

Generally speaking, I'd expect a lender to remove any adverse information recorded on a consumer's credit file as a result of the interest and charges on the loans they shouldn't have been given. After all it's the interest and charges that the consumer is being refunded and the expectation is they will have repaid, or they should repay what they owe. As the monetary award I'm making reflects this, I see no reason to depart from our typical approach in this case. So I think that 118 118 Money should remove any adverse information recorded on Mr S' credit file as a result of these loans.

All of this means that I think it would be fair and reasonable in all the circumstances of Mr S' complaint for 118 118 Money to put things right in the following way:

- add up the total amount of money Mr S received as a result of having been given his loans. The loan payments Mr S made should be deducted from this amount. Any payments made after the total repaid exceeds the amount of money Mr S was given should be treated as overpayments;
- add interest at 8% per year simple on the above overpayments from the date they were paid by Mr S to the date of settlement†;
- remove any adverse information recorded on Mr S' credit file as a result of these loans.

† HM Revenue & Customs requires 118 118 Money to take off tax from this interest. 118 118 Money must give Mr S a certificate showing how much tax it's taken off if he asks for one.

my final decision

For the reasons given above, I'm upholding Mr S' complaint. Madison CF UK Limited (trading as "118 118 Money") should pay Mr S compensation as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr S to accept or reject my decision before 5 March 2019.

Jeshen Narayanan
ombudsman