

The complaint

Mr N complains that he was unable to sell some of the loan parts in his crowdfunding account with Funding Circle Ltd.

What happened

Funding Circle is a loan-based crowdfunding platform which allows investors to lend money to prospective borrowers in return for interest payments. An investor agrees to lend a proportion of the total loan a borrower is looking to borrow, and in return an investor receives interest on their loan part. At the time of Mr N's complaint, Funding Circle provided an autosale tool on its platform. This provided a way for investors to access their funds early by selling their loan parts to other investors by way of a secondary market. But this was subject to the loan part meeting certain requirements, such as there not being a late payment or a default on the loan.

Mr N requested to sell around £3,000 of his investments in April 2019. Although Mr N was unhappy that it took until the 31 May 2019 for the sale to complete, he was also dissatisfied that he only received just over £1,200 from the sale. Funding Circle explained that this was because around 35 of the loan parts he put up for sale were removed from the sales queue before the sale was completed. Mr N complained to Funding Circle as he didn't understand why this happened.

Funding Circle explained that there were some restrictions on selling loan parts. It said that loan parts could not be sold when they were in a 'processing status' – where a borrower is within the direct debit cycle (for the purposes of making their regular interest payments) and the direct debit has not yet been received by Funding Circle in order for it to be distributed to lenders.

Funding Circle explained that some of Mr N's loan parts had entered into this processing status, which caused them to be removed from the sales queue (between the time he requested the sale and before they could be successfully sold to other investors). It explained that this restriction was an important way of protecting investors looking to buy loan parts on the secondary market, as it prevented loan parts from being sold where Funding Circle had not yet received the monthly repayment successfully from the borrower.

Funding Circle apologised for any disappointment it may have caused but explained that Mr N would be able to re-list any unsold loan parts after the repayments were successfully received and noted that he had done this. Whilst Funding Circle was confident that it made investors aware of the selling restrictions on the platform, it did acknowledge that the information about the possibility for loan parts to be removed from the sales queue mid-sale could have been made clearer to Mr N. And so it offered £25 in recognition for any inconvenience caused.

Mr N didn't accept Funding Circle's response as he felt it hadn't answered why all 35 loans had gone into a processing status on 30 May 2019, only to become eligible for sale again the following day. He thought it was highly unlikely that 35 failed direct debit payments were resolved within 24 hours and instead suggested that there was an issue with Funding Circle's processes.

Funding Circle explained that loans can go into a processing status when it has been unsuccessful in taking payments from the borrowers the first time around. It said that it looks to take the payment from the borrower before the payment date, and where there is a delay in receiving this, the loan will go into a processing status until Funding Circle re-requests the payment and it is successfully taken. Funding Circle also suggested that the recent bank holidays may have affected the payments.

Mr N remained unhappy as he felt Funding Circle's systems should be able to deal with bank holidays and he requested that it provide him with evidence that the borrowers failed to pay on time. However, Funding Circle was unable to provide this as it explained that records aren't kept for loans which temporarily go into processing status.

In June 2019 Funding Circle contacted Mr N to explain that it had updated its sale tool and the way that it operates. Previously it selected the loans for sale at the time when an investor put the sale request through, but it had since changed so that it selects available loans when an investor reaches the top of the queue instead. Funding Circle hoped that this would prevent loans from being removed from the queue when they go into a processing status before reaching the top of the queue.

Mr N was pleased with these changes but asked that our service investigate his complaint.

One of our investigators looked into Mr N's complaint but didn't think Funding Circle had done anything wrong. In short, she said:

- Funding Circle explained that during the waiting period to sell on the secondary market, any loan parts that weren't eligible for sale were removed from the sales queue.
- Funding Circle's terms and conditions made it clear when a loan wouldn't be eligible for sale.
- Once a loan part was removed it wasn't re-listed even if it became eligible for sale again.
- Funding Circle acknowledged that an investor would have to re-list and wait, hoping their loan parts didn't become ineligible for sale again whilst in the sales queue.
- Funding Circle's terms and conditions stated that, "*it may not always be possible to withdraw the exact amount of your request.*"
- Funding Circle had since made changes to their system based on feedback from investors.
- Funding Circle's terms and conditions explained that, "*you can sell your loan parts to other investors (subject to demand)*" and so being able to sell relies on other investors wanting to invest, which is out of Funding Circle's control.
- Overall, Funding Circle had addressed Mr N's concerns; its terms and conditions were clear; and the £25 offered felt fair.

Mr N didn't agree with the investigator. In summary, he felt it was too much of a coincidence that all 35 loans had failed repayments on them and were then suddenly resolved the following day. But if this was the case then he wanted to see evidence of this.

As an agreement couldn't be reached, the case was passed to me to decide.

Having passed the case to me for a decision, Funding Circle made further representations which explained:

- It received funds from the borrowers on Mr N's loan parts in question before 30 May 2019. But these weren't distributed to investors until 31 May 2019, a day after the actual repayment date. This is why the loans changed to processing status.
- This is standard practice across the platform and not an individual issue with Mr N's account.
- As there was a bank holiday on 27 May 2019, payments on loans which were due that day took priority on the following day when they were able to be processed, as the payments are processed in date order.
- Therefore, Mr N's loans were affected by the bank holiday, due to the increase of loans needing to be processed, causing a slight delay to all payments on loans which were due in the few days following the bank holiday.

I issued a provisional decision in August 2020. In it I said:

In reaching my provisional conclusions on this case, I've taken into account industry good practice, and any applicable guidance or rules from the FCA. These include high level principle 2.1 A firm must conduct its business with due skill, care and diligence, 2.7 communicate information in a way that is fair, clear and not misleading and COBS 2.1.1 A firm must act honestly, fairly and professionally according to the best interests of its client.

Funding Circle provides an opportunity for investors to sell their loan parts to other investors by way of the auto-sale tool on the platform. Although Mr N could use the auto-sale tool to request his loans parts to be sold, Funding Circle's terms and conditions set out some limitations to this. The terms and conditions explain that loan parts can't be sold, "if there is one repayment remaining" or "if the internal risk band classification of the [loan] has changed". They also explain that loans "which are late or in default" or loans "which are part of a loan securitisation exercise" are also unable to be sold.

Funding Circle's terms and conditions also explain that it can't guarantee that all the loan parts will sell, nor how long it may take for a sale to complete, as this is reliant upon there being a demand by other investors – something which I agree is out of Funding Circle's control.

So whilst Mr N is clearly unhappy with the amount of time it took for his sale request to be completed, the crux of the complaint, and in my view the main issue which I need to decide, is whether it was fair and reasonable for Funding Circle to remove some of his loan parts from the sales queue.

Funding Circle initially explained that it removed Mr N's loan parts from the sales queue as they had gone into a processing status due to borrowers not making their payments on time. However, Funding Circle has since clarified that payments were received into its account from the borrowers prior to the payment date. So it's my understanding that the loans went into a processing status because Funding Circle was unable to process the payments from borrowers and allocate these to investors by the payment date.

I appreciate that Funding Circle has said this was due to a knock-on effect of delays caused by the bank holiday, however, the fact remains that the borrowers' payments weren't late. I've also not been provided with any evidence to suggest that Mr N's loans were ineligible for transfer due to any of the other reasons listed under Funding Circle's terms and conditions. So it's clear Funding Circle acted outside of its terms and conditions by removing Mr N's

loan parts.

I've considered whether it was fair for Funding Circle to act outside of its terms and conditions in this instance and I'm not persuaded that it was. Funding Circle offered a service where Mr N could sell his loans if other investors on the platform were willing to buy them. Whilst I appreciate Funding Circle can't control demand, it ought fairly to process requests in a systematic and fair way. In Mr N's case, he asked to sell some of his loan parts and there was no fundamental reason why he should not have been able to. The loan parts didn't present some different level of risk to prospective investors, which would have been a fair reason for Funding Circle to withdraw them. The loan parts had the appearance of having something wrong with them, but this was purely down to the status Funding Circle applied to them. And this wasn't a fair reflection of the actual status of the loan parts because the repayments had indeed been received from the borrowers. So Mr N has been disadvantaged for no reasonable reason.

Considering all of the above, I'm currently minded to uphold Mr N's complaint. As such, I consider Funding Circle ought to compensate him.

putting things right

When looking to put things right, I must consider that even if Funding Circle hadn't removed Mr N's loan parts from the sales queue, it wasn't guaranteed that all his loan parts would have sold. This is because the sale of loan parts is dependent on there being other investors who want to take ownership of these. I'm conscious that Mr N's loans had already been up for sale for around a month and had not sold before being removed from the sales queue. So given the length of time they'd been up for sale, I can't say on the balance of probabilities when or even if the loan parts would have sold. As such, it isn't possible to attribute a financial loss to Mr N as a result of Funding Circle's decision to remove the loan parts from the sales queue.

However, I have also considered what impact Funding Circle's actions had on Mr N. And having done so, it's clear that Mr N has suffered some trouble and upset here. I think it was fair for Mr N to ask for a clear explanation as to why his loan parts were removed and I can see he invested a great deal of time in communicating with Funding Circle to get an answer. However, Funding Circle wasn't able to provide him with the detail he was hoping for which I understand would have caused him further frustration. I also appreciate that Mr N had to go through the inconvenience of having to put the loan parts back up for sale again which he wouldn't have needed to do had the borrowers' payments been processed on time, but for Funding Circle's delay. Taking all this into account, I'm satisfied that Funding Circle's error caused Mr N trouble and upset for which I consider £150 to be fair and reasonable compensation.

In response to my provisional decision, Funding Circle acknowledged that its system failed to account for the delay in receiving and redistributing loan repayments that were due over a bank holiday, which resulted in Mr N's loan parts being flagged as processing. So it agreed to compensate Mr N £150 for the level of inconvenience he experienced.

However, Funding Circle rejected my findings on the basis that it didn't think Mr N had been treated unfairly. In summary, it said:

- It's critical from both a legal and regulatory perspective, but also from a customer protection perspective that it detects all late or missed payments on loans and suspends the affected loan parts from being sold on the secondary market.
- If a business is late in repaying, or if Funding Circle has any other information which might suggest that the repayment status of the loan or the creditworthiness of the

borrower has changed or is changing, it is obliged to act. And a failure to do so would put it in breach of its regulatory obligations.

- It cannot monitor this manually, on a loan by loan or transaction by transaction basis, therefore it is not unreasonable for it to have implemented automated rules and triggers which act to protect investors.
- With all automated systems, they are designed to include an extra element of caution to protect the customer from any potential risks. It is preferable in product design to have occasional 'false-flags' than to miss incidents which ought to have been identified. Where these anomalies arise, the occasional undesirable outcomes are preferable to the alternative.
- Whilst it acknowledged that the product is not perfect, and it had since fixed the bank holiday issue, it said it did not treat Mr N in a way that is contrary to its terms and conditions or other published investor guidance - all of which make it clear that the availability of the secondary market is not guaranteed and that there is no obligation on Funding Circle to act on any sale request if it believes it has good reason not to.
- With hindsight, it acknowledged that in Mr N's case there was no additional risk attached to those loan parts that were unable to be sold, but in almost all other cases where a loan changes to a processing status, the reason behind the status change is due to a failure on the borrower's part to make repayments on time. Therefore, the processing status is a fundamental control that has been implemented with our investors' protection in mind.

Mr N accepted my findings in the provisional decision and accepted the £150 compensation which I'd recommended.

What I've decided – and why

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

Having done so, I see no reason to depart from my provisional conclusions.

I'm pleased to see that Funding Circle has agreed to compensate Mr N £150 for the trouble and upset caused, as outlined in my provisional decision. However, I understand it disagrees that Mr N was treated unfairly. I believe many of the points Funding Circle has made have been made previously and that I've already taken them into account and addressed them in my provisional decision. So they don't change my thoughts on the case, and I won't repeat my reasoning at length here.

However, having reviewed Funding Circle's comments, there are some areas that I would like to clarify.

I appreciate the points Funding Circle has made regarding the regulatory need to have a system in place to prevent loan parts being sold on the secondary market where there are repayment issues. I agree that this is a fundamental safeguard for the protection of investors who purchase these loan parts. I also accept that Funding Circle may not be able to monitor this on a loan by loan or transactional basis and so it relies upon automated systems for detection.

However, it's clear to me that this automated system didn't work as intended in Mr N's case. Funding Circle's terms and conditions allow it to remove loan parts from the secondary market which are late or in default. But as previously explained, this clearly wasn't the case here. Funding Circle has accepted that its system failed to account for the delay in receiving and redistributing borrowers' repayments which were due over the bank holiday period. This meant that Mr N's loan parts weren't dealt with as they should have. And this resulted in Mr

N being in a position he oughtn't have been in, but for this system feature. It's therefore fair and reasonable for Funding Circle to compensate him for any financial loss or trouble and upset he suffered as a result.

Whilst I understand Funding Circle's logic that it's preferable to have the occasional 'false-flags' than to miss incidents which ought to have been identified, the fact remains that there were false-flags which caused Mr N detriment and so he ought to be compensated for this.

As explained in my provision decision, Funding Circle never guaranteed that Mr N's loan parts would sell on the secondary market, a point it makes clear in its terms and conditions. And since Mr N's loans had already been up for sale for around a month and had not sold before being removed from the sales queue, I can't say on the balance of probabilities when or even if the loan parts would have sold. As such, it isn't possible to attribute a financial loss to Mr N as a result of Funding Circle's decision to remove the loan parts from the sales queue.

However, it's clear that Mr N suffered some trouble and upset here. I think it was fair for Mr N to ask for a clear explanation as to why his loan parts were removed and I can see he invested a great deal of time in communicating with Funding Circle to get an answer. However, Funding Circle didn't provide him with the detail he was hoping for which I understand would have caused him further frustration. I also appreciate that Mr N had to go through the inconvenience of having to put the loan parts back up for sale again which he wouldn't have needed to do had the borrowers' payments been processed on time, but for Funding Circle's delay.

Taking all this into account, I'm satisfied that Funding Circle's error caused Mr N trouble and upset for which I consider £150 to be fair and reasonable compensation.

My final decision

My final decision is that I uphold this complaint. Funding Circle Ltd must pay Mr N £150 compensation for the trouble and upset caused within 28 days of when we tell it Mr N has accepted my final decision.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr N to accept or reject my decision before 7 November 2020.

Ben Waites
Ombudsman