

The complaint

Miss H complains that First Response Finance Ltd (FRFL) irresponsibly entered into a hire purchase agreement with her. She says she was struggling financially at the time.

What happened

In April 2020 FRFL provided Miss H with finance to purchase a used car. The car cost £5,495 and Miss H paid a deposit of £495. She entered into a hire purchase agreement to finance the remaining £5,000. After interest and charges the total amount due was £9,569.68, repayable in 61 monthly instalments of £156.88.

In April 2023, Miss H complained to FRFL saying that they didn't consider her application properly, and had they done so they would have seen she couldn't afford the monthly repayments. She said she felt FRFL had taken advantage of her situation by charging her a high rate of interest.

FRFL didn't agree with Miss H's complaint. They said they carried out proportionate checks before agreeing to lend, including a full credit search, income verification via payslips and bank statements, and using statistical data and information provided by Miss H about her non-discretionary expenditure. FRFL felt their checks showed Miss H had enough disposable income after meeting all her commitments to be able to afford the monthly repayments.

Miss H disagreed and referred her complaint to the Financial Ombudsman Service, where it was considered by one of our investigators. They thought FRFL's checks were proportionate in the circumstances and that FRFL made a fair lending decision. They didn't think the complaint should be upheld. Miss H didn't agree with our investigator's view. She said FRFL had ignored a County Court judgment (CCJ) and frequent pay day loans she was relying on at the time. She also asked if FRFL operated a discretionary commission model at the time she took out the agreement.

Our investigator contacted FRFL and confirmed that the CCJ had been noted, but due to the time that had passed since it had been entered, and the low amount involved, FRFL were happy to proceed. FRFL also confirmed that they had never used discretionary commission models. The investigator didn't think the additional information changed the overall outcome, so Miss H asked for an ombudsman's decision – and the complaint came to me.

I issued a provisional decision on 4 April 2024, saying I was inclined to uphold Miss H's complaint. In that I said:

“The Financial Conduct Authority (FCA) sets out in a part of its handbook known as CONC what lenders must do when deciding whether to lend to a consumer. In summary, a firm must consider a customer's ability to make repayments under the agreement without having to borrow further to meet repayments or default on other obligations, and without the repayments having a significant adverse impact on the customer's financial situation.”

CONC says a firm must carry out checks which are proportionate to the individual circumstances of each case. When determining what's proportionate, we'd expect lenders to think about the nature of the credit (the amount repayable and the term, for example) and about the applicant's individual circumstances. I'd expect a lender to find out more about a prospective borrower's ability to repay if for example, a borrower's income was low, the amount lent was high, or the borrower's credit file reveals an impaired credit history.

Were FRFL's checks proportionate?

I've thought about the checks FRFL carried out. FRFL's records show that at the time of application, Miss H was single with one dependent child, and she was a council tenant. Miss H said she'd been working for the NHS for almost three years.

FRFL looked at Miss H's credit file and discussed the outcome of it in a telephone interview with her. They verified her declared income using both payslips and bank statements and estimated Miss H's expenditure using a combination of statistical data, her own testimony and information obtained from her bank statements.

Although Miss H's credit file showed that she'd experienced some financial difficulties, including defaults and a CCJ, there are no further checks I'd expect FRFL to have made. I say this because the evidence FRFL gathered gave them enough information to get a thorough understanding of Miss H's finances to help them determine if the lending was affordable and sustainable.

I think it would be helpful here to explain that having an impaired credit history doesn't mean FRFL shouldn't lend. And FRFL specialises in lending to those who might otherwise struggle to obtain finance because of their credit rating. Miss H said FRFL took advantage of her situation by charging higher interest. But the rules in place at the time allowed FRFL to decide the terms on which they were prepared to lend, including what interest rate they would charge.

Did FRFL make a fair lending decision?

Looking at Miss H's circumstances and the terms of proposed agreement, I'm satisfied FRFL's checks were proportionate. I've gone on to consider if FRFL made a fair lending decision.

Miss H declared her income as being £1,220 per month, and said she was expecting this to increase by £100 per month going forward. FRFL didn't include this potential increase in their calculation, which I think was reasonable. They asked Miss H about the impact of the Covid-19 pandemic on her working hours, and she confirmed that they hadn't changed. FRFL looked at Miss H's payslips and calculated her average monthly wages to be around £1,128. They used this figure in their income and expenditure assessment.

Miss H received tax credits of £131 per week on average – around £570 per month. And FRFL confirmed this during their phone interview with Miss H. I note that FRFL included child benefit in Miss H's income, at around £89 per month. This shows in the 'advised' column of their income calculation, which suggests it is information Miss H gave FRFL as part of her application.

FRFL were able to verify Miss H's tax credits using her bank statements. However, when looking at Miss H's bank statements I couldn't see child benefit credited to her account in the three months prior to the agreement. I haven't seen any evidence to

show FRFL verified this element of Miss H's income. I don't think they should have included it without having verified it – CONC says a firm shouldn't rely solely on a customer's own statement of their income.

FRFL said Miss H's average monthly income was around £1,787. Taking out the child benefit would reduce this figure to around £1,698.

During the phone interview, FRFL asked Miss H about her housing costs, and she confirmed she paid just under £500 in rent and council tax. FRFL used statistical data to estimate Miss H's other costs of living, which the rules in place at the time allowed them to do. They estimated this to be £490 and it included a provision for Miss H's child.

FRFL didn't set out what the cost of living figure includes, but I'd expect this to cover the monthly cost of groceries, utilities, communications, fuel, insurance and road tax. Looking at Miss H's bank statements, I've not seen anything to suggest it was inappropriate for FRFL to rely on the estimate they used. FRFL asked Miss H about some specific costs, and she confirmed she spent £20 a week on childcare and that her motor insurance for the new car would be £57 per month. I think FRFL's overall assessment of Miss H's cost of living, at around £1,132, was fair.

FRFL's credit check showed Miss H had two credit cards with a total balance of around £360, a mail order account with a balance of around £257 and an unsecured loan and home credit with a combined total of around £4,840. FRFL calculated Miss H had monthly credit commitments of around £327. They also added an additional £6 for a debt portfolio payment, which FRFL had noted on review of Miss H's bank statements.

I can see that for the unsecured loans and home credit FRFL used the monthly repayment as shown on Miss H's credit report. This includes £23 for one home credit agreement, but I note that the agreement came to an end in April 2020 and therefore no further payments would be due under it. For the revolving credit and defaults however FRFL allowed a monthly repayment of 3% of the outstanding amount. This would only see Miss H making minimum repayments towards her outstanding debt. CONC requires a firm to assume that revolving credit is repaid over a reasonable term. I'm inclined to say FRFL should have used at least 5% of the outstanding amount to reflect that.

In addition, FRFL only included repayments for debts shown on Miss H's credit file. Her bank statements show payday lending and weekly repayments to two providers which FRFL don't appear to have taken into consideration. FRFL should have included the repayments in their income and expenditure assessment. Overall, I think FRFL ought to have allowed £406 to meet Miss H's monthly credit commitments. This figure includes the payday loan repayments and an increase from 3% to 5% on existing credit but excludes the £23 repayment for the home credit agreement that was about to end.

I've noted Miss H's comments about using payday loans and an unsatisfied CCJ, which FRFL didn't address in their final complaint response. And I could see there's a dispute about the CCJ. FRFL said their check indicated the CCJ had been satisfied, but Miss H said it wasn't. She's provided information she received during a data subject access request from another business, which shows an active, unsatisfied CCJ in February 2020. But I don't think I need to reach a finding here, and that's because I think that, even excluding the CCJ, the lending was unaffordable.

I say this because I think FRFL should have calculated Miss H's average monthly income to be around £1,698 and her outgoings as approximately £1,538, leaving her with disposable income of £160 before taking into consideration the proposed repayment of £156.88 per month. This would have left Miss H with very little to cover any unforeseen expenditure.

Overall, I'm inclined to say FRFL didn't make a responsible lending decision. It should have been clear to them that Miss H wouldn't be able to sustainably make repayments under the agreement. It follows that FRFL shouldn't have lent to Miss H."

Miss H accepted my provisional decision. FRFL disagreed and said, in summary:

- Miss H never said she wasn't in receipt of child benefit. And given she was receiving other benefits and was eligible for child benefit, it's likely she did receive it – possibly into a different account.
- There was no rule in place stating lenders had to assume 5% repayments for revolving credit.
- Miss H needed the vehicle for work, and not lending to her could have landed her in a worse position than had FRFL not agreed the lending.
- Miss H maintained the payments under the agreement, and it wasn't until she raised her complaint that affordability was called into question.

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'm upholding Miss H's complaint. I'll address FRFL's additional comments in turn.

In my provisional decision, I said it was possible Miss H told FRFL she was receiving child benefit. But FRFL should have verified this rather than simply relying on what Miss H said, or an assumption. The bank statements they've seen don't show child benefit, and I've not seen evidence to show FRFL made further enquiries when they weren't able to verify this element of Miss H's income.

I remain satisfied that FRFL should have calculated Miss H's likely outgoings as £1,538 per month, including revolving credit balances repaid at 5% of the outstanding balances per month. I've thought carefully about what FRFL said about the rules in place at the time. FRFL also said making minimum repayments was acceptable and wouldn't lead lenders to take action against Miss H. CONC requires lenders to assume that revolving credit is repaid over a reasonable term. Only making minimum repayments each month is unlikely to achieve this – and so the expectation is that lenders assume repayments above the minimum amount. I accept CONC doesn't set out what that should look like in practice. But I'm satisfied that 5% of the outstanding balance is reasonable.

So, even if I were to include child benefit in Miss H's net monthly income, it would leave her with just over £90 disposable income after her committed and non-discretionary spending and the payments due under this agreement. This wouldn't have left her with much to cover any unforeseen or emergency expenditure.

I don't dispute that Miss H needed a car – and I think that's likely why Miss H ensured she kept up with the monthly repayments. But it's FRFL's obligation to lend responsibly – and if they can't demonstrate that lending is affordable, they shouldn't agree to lend. If FRFL had

decided not to lend to Miss H, she could have explored other options such as seeking a cheaper car or using alternative methods of transport.

In summary, I find that FRFL didn't make a fair lending decision, because the evidence they collected ought to have shown Miss H couldn't afford the repayments due under the agreement in a sustainable way. For this reason, I uphold her complaint.

Putting things right

As FRFL shouldn't have approved the lending, it's not fair for them to charge any interest or charges under the agreement. But Miss H has had use of the vehicle, so it's fair she pays for that use. I'm not persuaded that monthly repayments of over £156 a month are a fair reflection of what fair usage would be. This is because a significant proportion of those repayments went towards repaying interest. It appears that Miss H has already paid more than the cash value of the vehicle to FRFL. So it's fair she keeps the car and FRFL refund everything above the cash price.

To settle Miss H's complaint FRFL should do the following:

- End the agreement with nothing further to pay, and transfer ownership of the vehicle to Miss H.
- Calculate how much Miss H has paid in total and deduct £5,000 for the cash price of the vehicle. FRFL should refund any overpayments, adding 8% simple interest per year* from the date of each overpayment to the date of settlement.
- Remove any adverse information recorded on Miss H's credit file regarding the agreement.

*HM Revenue & Customs require FRFL to take off tax from this interest. FRFL must give Miss H a certificate showing how much tax they've taken off if Miss H asks for one.

My final decision

For the reasons given above, I'm upholding Miss H's complaint. First Response Finance Limited need to settle the complaint as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Miss H to accept or reject my decision before 6 June 2024.

Anja Gill
Ombudsman