DRN-4479162

The complaint

Mrs B is complaining that Specialist Motor Finance Limited (SMF) shouldn't have lent to her – she says they were irresponsible in doing so. Mrs B brought her complaint to us via a representative, but for ease I've written as if we've dealt directly with her.

What happened

In June 2019, Mrs B took out a hire purchase agreement with SMF to finance the purchase of a vehicle. She paid a deposit of £5 and borrowed £5,995 – the cash price of the vehicle was £6,000. The agreement required Mrs B to make 59 monthly repayments of £166.99, followed by a final instalment of £176.99 (including a £10 option to purchase fee).

In July 2022, Mrs B complained to SMF, saying that she thought SMF had failed to conduct appropriate checks before lending to her. She said she had a number of active credit agreements at the time of the lending as well as two defaulted accounts and two further accounts which had defaulted and been passed to debt recovery companies.

In response, SMF said when she'd applied, Mrs B told them she earned £1,500 net monthly income, was married, and lived in rented accommodation. They said they verified her income but didn't explain how. SMF added that they'd carried out a credit check before lending to Mrs B, but as they specialise in providing credit to people who've previously experienced financial difficulty, some level of missed payments on credit wouldn't be a reason for them to decline an application.

SMF went on to explain how they'd calculated that the loan was affordable for Mrs B – saying they'd factored in her credit commitments and split the rent and cost of living amounts because she was married. They said the maximum monthly payment they would have allowed Mrs B was £375 so the actual repayments of £167 were within her capacity.

Mrs B was unhappy with SMF's response and brought her complaint to our service, where one of our investigators looked into it. SMF provided some more information about the affordability checks they had done but our investigator upheld the complaint, saying she thought SMF hadn't done enough to check that the lending was affordable for Mrs B.

SMF didn't reply to our investigator's view, so the complaint's been passed to me for a decision.

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 Mrs B's complaint for broadly the same reasons as our investigator – I'll explain below.

The Financial Conduct Authority (FCA) sets out in a part of its handbook known as CONC what lenders must do when deciding whether or not 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.

Did SMF carry out proportionate checks?

SMF said they carried out the following checks:

- reviewed Mrs B's credit file;
- used current account turnover analysis and other checks from one of the credit reference agencies to verify that Mrs B hadn't overstated her income; and
- used statistical data to estimate Mrs B's cost of living and hence disposable income. SMF added that they then cap this figure depending on various factors and in Mrs B's case it was capped at 25% of her net monthly income, i.e. £375.

Whether or not these checks were proportionate depends on various factors, including the size and length of the loan, the cost of credit, and what SMF found. At around 25%, the cost of credit was significant, and the term of the loan was five years. So I'd expect the checks to be thorough.

SMF said they verified Mrs B's income as £1,500 per month, took her monthly credit payments figure of £73 from her credit file and estimated her cost of housing as £394, and other cost of living expenditure as £297. They said these estimates were based on data from a credit reference agency and assumed Mrs B and her husband shared these costs equally.

CONC allows a business to use statistical data when it hasn't got reasonable cause to suspect the statistical data might not be appropriate. But when SMF looked at Mrs B's credit file, they'd have seen she had defaulted on four accounts and two of these defaults had been just four months prior to her application. She'd also missed a payment on a credit card six months before her application. SMF's estimates suggested Mrs B had disposable income of over £700 per month – but this isn't consistent with someone having recent defaults and missed payments on their credit file.

On balance I'm not satisfied SMF carried out proportionate checks – in the context of the recent defaults I think they should have done more to understand Mrs B's expenditure.

If SMF had done proportionate checks, what would they have found?

I've looked at statements for Mrs B's bank accounts for the three months leading up to her application to SMF. I'm not saying SMF needed to obtain bank statements as part of their lending checks. But in the absence of other information, bank statements provide a good indication of Mrs B's expenditure at the time the lending decision was made.

Looking at these statements, I can see Mrs B was using a significant amount of credit – her payments to creditors were much higher than SMF had estimated, averaging around £540 per month. Mrs B had limited other committed expenditure – she was paying around £160 per month for TV, phone, internet, and pet insurance, and paying around £200 per month to another individual which appears to have been a contribution to rent and bills. On top of this, she was spending around £350 per month on food and fuel. So in total, Mrs B's non-discretionary and committed expenditure totalled around £1,250.

As SMF found, Mrs B had income of around £1,500 per month. And the monthly repayments under their agreement were around £170. So it would be fair to assume Mrs B would have monthly disposable income of around £80 after taking out this agreement. I'm not satisfied this was enough to cover emergencies and any additional expenses arising from having a new vehicle.

In addition, I note Mrs B was often in her overdraft, and used multiple different lenders for short-term credit. It's clear she wasn't managing her existing credit repayments in a sustainable way, which adds weight to my decision that this new agreement wasn't affordable for her. If SMF had done proportionate checks they couldn't have fairly decided to lend to Mrs B.

Putting things right

As I don't think SMF should have approved the loan, I don't think it's fair for them to charge any interest or other charges under the agreement. But Mrs B has had use of the vehicle for over four years and it's fair she pays for that use. Mrs B has now paid more than the cash price of the car – I'm satisfied that's enough to reflect fair usage.

To settle Mrs B's complaint, SMF should do the following:

- End the agreement with nothing further to pay and transfer ownership of the vehicle to Mrs B.
- Refund all the payments Mrs B has made in excess of £6,000 (the cash price of the car), adding 8% simple interest per year from the date of each overpayment to the date of settlement.
- Remove any adverse information recorded on Mrs B's credit file regarding the agreement.

If SMF consider tax should be deducted from the interest element of my award they should provide Mrs B a certificate showing how much they've taken off so that Mrs B can reclaim that amount, assuming she is eligible to do so.

My final decision

As I've explained, I'm upholding Mrs B's complaint. Specialist Motor Finance Limited need to take the steps outlined above to settle the matter.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs B to accept or reject my decision before 28 December 2023.

Clare King
Ombudsman