

## Irresponsible lending

We occasionally receive complaints alleging that a participant in our scheme has lent money to a customer who had no, or limited, ability to make the required repayments on the loan when they took it out. To lend without sufficient regard to the customer's ability to repay is known as "irresponsible lending".

For us to find that a banking service provider has lent irresponsibly, we must be able to show that it knew, or should have known, that the customer could not afford the loan repayments at the time they requested the loan, or when the loan was drawn down.

We use the same approach whether the lending is secured or unsecured. It can be any type of lending including mortgages, personal loans, business lending, credit cards and authorised overdrafts.

### How do we approach these complaints?

Under the Code of Banking Practice, banking service providers must only provide credit or increase a customer's credit limit when the information they have available leads them to believe that the customer will be able to meet the terms of the lending. All participants in the Banking Ombudsman Scheme must observe the Code of Banking Practice.

Our terms of reference allow us to investigate complaints about the "administration" of a lending decision. This basically means we can look into a number of aspects around how the decision was made that may lead us to a finding of irresponsible lending. We can't, however, investigate a banking service provider's commercial decision to lend.

### What factors do we take into account?

When we are considering an allegation of irresponsible lending, we look at a number of factors.

- What information did the banking service provider ask for and what did it receive about the customer's ability to repay?
- Did the banking service provider consider all the information available to it?
- Did the banking service provider comply with its own policies and procedures on credit assessment?
- Did the banking service provider waive a particular policy requirement, and if so, why?
- Was there anything that should have prompted the banking service provider to seek more information?

### How to contact us

A banking service provider must consider all relevant information available to it when making a decision to lend. It is not enough, for example, for a banking service provider to only consider a customer's repayment history when it also holds income information. The fact that a customer has met payments on a current credit facility may not, in itself, establish that the customer can repay a higher level of debt. The banking service provider may hold relevant information about the customer across various departments. It may not be enough for a banking service provider to only consider information held by the credit card department when other departments also hold relevant information.

Generally, we are unlikely to find a banking service provider has acted irresponsibly in approving an application for credit where the customer:

- actively seeks a loan
- is not under any sort of disability
- either meets the banking service provider's usual lending criteria, or is not far from it, and the banking service provider has made appropriate enquiries.

We are also unlikely to find that a banking service provider acted irresponsibly if:

- the banking service provider asked all the right questions and the questions were appropriately worded
- the customer didn't provide all the information they should have about their financial position or gave inaccurate responses.

## **What happens if we find a banking service provider's lending was irresponsible?**

If we find that a banking service provider has lent irresponsibly, but the customer has benefitted from the loan (for example, they have purchased a property that they want to keep), then we generally recommend that the banking service provider writes off all interest and charges associated with the loan. This is on the basis that the customer should not have to bear the cost of the borrowing.

In most cases, the customer will still be responsible for repaying the amount they borrowed, and we will generally encourage the banking service provider and the customer to enter into a repayment programme that the customer is able to afford.

In cases where there is no possibility of the customer making any repayment of the credit facility, we may ask the banking service provider to write off the debt. When this happens, the banking service provider may make an adverse credit listing against the customer to prevent that person's future access to credit for a period.

## **Where to find out more**

We have included a few case notes about irresponsible lending below. You can find other case notes on our website at [www.bankomb.org.nz/eng/Case-notes](http://www.bankomb.org.nz/eng/Case-notes)

Or you can call our enquiries team on 0800 805 950 to discuss how to make a complaint.

### **How to contact us**

## Case studies on irresponsible lending

### Irresponsible lending with credit card debt

A bank granted a customer a credit card account with a limit of \$3,000 but declined an application for a personal loan because he lacked the ability to service the loan. The customer was on an invalid's benefit and had a gambling problem. The bank later increased the credit limit to \$7,000. Two years later, the customer's parents advised the bank that their son had mental health and gambling problems. Despite this, the bank increased the limit to \$9,500. We found that there had been irresponsible lending. As a result, the bank refunded all interest it had already charged on the debt and agreed not to charge any interest on the remaining debt. We also recommended the bank pay compensation for inconvenience suffered by the customer.

A bank made a pre-approved credit card offer to two customers who were joint account holders. One of the customers accepted the offer. The bank had no information about the customer's ability to repay. If it had made enquiries, the bank would have discovered the customer had a mental incapacity which affected her ability to manage debt. We found that there had been irresponsible lending. As a result, the bank wrote off all interest and charges on the debt and arranged an affordable repayment programme.

### Irresponsible lending with mortgage loans

A bank granted a customer two separate loans several months apart totalling \$425,000. The loans were to buy sections of land. The customer struggled to meet the loan repayments and eventually sold both sections, but with a shortfall of \$200,000. The customer declared himself bankrupt.

The customer accepted that he was a willing borrower, but felt that the bank should have helped by saying declining his application. The customer here was also not a totally innocent party as he had not been entirely truthful on his loan application.

We noted that the bank's file held no information to support the customer's claims about the various assets he said he owned. In addition, the income information was a one sentence note from his employer stating that it was envisaged that the customer would earn \$150,000 over the year.

We found that the bank should have queried the information supplied. Had it done so, it would have discovered that the customer's income was uncertain and that he did not own one of the properties he had listed as an asset. The bank did not have enough information to reach a reasonable conclusion that the customer was able to meet the terms of his loan agreements. However, we didn't recommend a remedy in this case as the customer was bankrupt and the bank had written off the debt owed.

### Irresponsible lending not found

Mr and Mrs L were approached by a property development company with an investment proposal and decided to buy three investment properties in Auckland. The company introduced them to a mortgage broker who said that she would arrange the deposit for them.

The mortgage broker submitted a lending application for the deposit to the bank. The bank declined the application telling the mortgage broker that Mr and Mrs L did not have sufficient income. The mortgage broker then sent the bank a letter from a fictitious tenant confirming that they were renting Mr and Mrs L's holiday house. On the basis of the extra income, the bank approved the loan.

Mr and Mrs L drew down the loan for the deposit and paid it over to the company but the company collapsed some months later. Mr and Mrs L attempted to make loan payments for a while, but this caused them financial hardship. They had expected that all expenses related to the purchase would be met by rental income.

Mr and Mrs L complained that the bank should not have approved the loan because they did not have enough income to service the debt.

We found that the bank was not responsible for Mr and Mrs L's loss. The bank's lending process was sufficiently robust to meet its obligations under the Code of Banking Practice: it had initially declined the loan on the basis of the information provided; neither the bank nor Mr and Mrs L knew the mortgage broker had submitted a statement from a fictitious tenant to support their lending application; and the bank was not responsible for the actions of the mortgage broker.

## How to contact us

Freephone 0800 805 950 Email [help@bankomb.org.nz](mailto:help@bankomb.org.nz)  
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