

Concerns about lending decisions

June 2015

We receive a number of complaints about banks' lending decisions. What might be surprising is that we receive complaints about banks both refusing to lend and allowing customers to borrow when the customers say they could never have afforded the repayments.

Lending decisions are usually a matter of the bank's commercial judgement, which is outside the Banking Ombudsman Scheme's terms of reference, so we may not always be able to investigate. We can, however, investigate administrative errors in the lending application process. This may include two complaints around refusing to lend and what is sometimes termed "irresponsible lending".

When a bank considers an application for lending, amongst other things, it should take into account what the customer's income is and whether it is secure, what other debt the customer has to service, and the customer's credit rating.

Banks rely on being provided with honest and accurate information. Usually, a customer is required to sign a declaration confirming that the information they have given in support of their application is accurate. However, if the information is incomplete or if there is something on the face of the application that suggests the information is incorrect, the bank should make further enquiries.

For us to make a finding that a bank lent to somebody who lacked the means to meet loan repayments, we must be satisfied that the bank knew, or should have known, the customer could not afford the loan repayments when 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 overdrafts.

On the other hand, for us to find that a bank has acted incorrectly in refusing lending, we have to be satisfied there was an administrative failure in the bank's assessment of the lending application.

Our approach to complaints about lending / refusing to lend

All lenders including banks must only provide credit or increase a customer's credit limit when the information they have available leads them to believe the customer will be able to meet the terms of the lending.

Our terms of reference allow us to investigate complaints about the "administration" of a lending decision. This means we can look into a number of aspects around how the lending decision was

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made. Our terms of reference do not allow us to investigate a banking service provider's commercial decision around lending or refusing to lend.

Factors we take into consideration

When we are considering complaints about lending, we look at a number of factors:

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

A bank must consider all relevant information available to it across departments when making a decision about lending. For example:

- it may not be enough for a bank to only consider credit card department information when other departments also hold information relevant to a loan application
- the fact a customer has previously met payments on a current credit facility may not in itself, establish the customer can repay a higher level of debt so the bank may check other information it holds on that customer.

Generally we are unlikely to find in the customer's favour in a complaint about a bank's decision to approve a lending application when the customer was subsequently unable to service the loan, if the customer:

- actively sought a loan
- was not under any sort of disability, or affected by a disability at the time
- either met the bank's usual lending criteria, or was not far from it, and the bank made appropriate enquiries.

We are also unlikely to find in favour of the customer if:

- the bank 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.

When a complaint about a decision to lend is upheld

If we find a bank has lent to somebody who is unable to meet loan repayments, but the customer has benefitted from the loan (for example, they have purchased a property they want to keep), then we generally recommend the bank writes off some or all of the interest and charges associated with the loan. This is on the basis the customer should not have to bear the total 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 the customer is able to afford.

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In cases where there is no possibility of the customer making any repayment of the credit facility, we may ask the bank to write off the debt. When this happens, the bank may make an adverse credit listing against the customer to ensure all potential future lenders are aware that the customer has previously defaulted on lending.

When a complaint about a refusal to lend is upheld

We cannot require a bank to approve a lending application, as the decision to approve or decline lending is a matter of a bank's commercial judgment. Banks are, however, expected to follow an appropriate administrative process, in assessing these applications.

If we find that the bank has made an administrative mistake in assessing a lending application, for example, it has made a mistake about the applicant's level of income, we will ask the bank to reassess the application using the correct information.

Home loan applications affected by loan to value ratio (LVR) restrictions

It is possible the Reserve Bank's loan-to-value ratio restrictions requiring banks to restrict new residential mortgage lending of more than 80% of a property's value to no more than 10% of all new mortgage lending, may result in banks declining more low-deposit home loan applications.

For more information, see our [quick guide on the Reserve Bank's loan to value restrictions](#). We also have a [quick guide on guarantees](#) which contains useful information for people considering guaranteeing somebody else's borrowing. The [Reserve Bank website](#) also has information about loan-to-value lending restrictions.

If you wish to make a lending complaint, you can call our enquiries team on 0800 805 950 to discuss how to go about it.

Case notes

Irresponsible lending

The bank gave Mr J's son a \$10,000 bank loan to buy a car. He was 19, on a 90-day trial period for a new job and paying \$150 weekly board from a modest income.

Shortly after, the son left his job and could not repay his loan. He was then jailed for an unrelated offence.

In Mr J's view, the bank would not have lent to his son if it had undertaken appropriate credit and criminal checks, enquired into his account conduct and if it had sought confirmation that his son was living rent-free as claimed. It should also not have approved the loan because he was on trial period at work, with no guarantee of continued employment.

In response the bank said:

- the son met its standard lending criteria

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- it was not standard practice to obtain customer criminal records before lending, or to speak with a loan applicant's family
- it had no evidence from account transactions, or elsewhere, that the son paid board because he paid cash.

Mr J was not satisfied and complained us. We cannot investigate commercial decisions about lending, but can investigate irresponsible lending allegations. We consider lending is irresponsible if information available at the time of lending indicates the customer may be unable to make required repayments.

In this case, we could not find irresponsible lending because:

- repayments were affordable based on information the son provided
- the bank did an appropriate credit check
- the bank was entitled to assume application details were accurate as it had no information to suggest otherwise
- the bank was not obliged to confirm details with Mr J or his family.

We also considered we were unable to interfere with the bank's commercial judgment to lend to someone who in all other respects met its lending criteria but was on a 90-day trial period. Similarly, banks can decide whether a person's previous account conduct meets lending criteria.

Declined lending

Mr and Mrs E approached their New Zealand bank for a loan to buy a property overseas. They claimed two bank officers told them there would be no problem and so they signed a contract to buy the property.

However, the bank declined their formal loan application, as a property offered as security was in a leaky building. Mr and Mrs E claimed the bank officers knew about this when giving the verbal approval because three months earlier the bank approved a loan for their contribution to building repairs.

The bank confirmed it held information about the leaky building loan application but that this information was not available to the bank officers when speaking to the complainants. It said neither bank officer gave any indication the loan would be approved. It also said it did not decline the loan outright, but sought further information about the leaky building repairs progress and costings. As Mr and Mrs E did not provide this, the loan did not proceed.

Mr and Mrs E complained to us about the bank's decision not to lend.

Having listened to a phone recording of Mr and Mrs E's first conversation with the bank about the loan, we found that the bank officer did not indicate it would be approved – he said it would need to be assessed against the bank's normal lending criteria. The leaky building issue was not discussed.

We did not agree that the bank was unreasonable asking for further information about the apartment when it already held information from the earlier loan application. The two lending propositions were different: the repairs loan was smaller with plenty of security while the UK property loan was much larger. Moreover, the bank did not have an updated residential property valuation and the property offered as security was in a leaky building.

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We also discovered that Mr and Mrs E had signed the contract to purchase the UK property two days after the bank stopped progressing their application. They appeared to have done this knowing the bank was not prepared to provide finance at that time.

Finally, Mr and Mrs E believed the bank's lending criteria was unduly restrictive. We advised them we had no power to investigate a complaint about a bank's commercial judgement in a lending or security situation, or to require a bank to change its criteria. The bank's decision to turn down the loan or stop progressing it was based on a concern about the value of the security offered.

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