

## **AMI response to Consultation Paper CP 10/5 Regulatory fees and levies 2010/11**

### **Introduction**

This response is submitted on behalf of the Association of Mortgage Intermediaries (AMI). AMI is the trade association representing over 75% of UK mortgage intermediaries.

Intermediaries active in this market act on behalf of the consumer in selecting an appropriate lender and product to meet the individual consumer's mortgage requirements. Our members also provide access to associated protection products.

Our members are authorised by the Financial Services Authority (FSA) to carry out mortgage and insurance mediation activities. Firms range from sole traders through to national firms and networks with thousands of advisers.

### **The need for change**

The fees proposals for the mortgage intermediary sector mean that AMI members will see an increase in regulatory costs of 33% overall this year. Based on what firms were charged last year, a £500,000 turnover firm is looking at a 32% increase whilst a £5 million turnover firm will see an 87% increase. At the same time, the A2 Home Finance Providers fee block will see its annual funding requirement (AFR) reduce from £10.3m to £9.6m. In our view, this proposal is inequitable.

The total AFR for the industry (A2 and A18 but excluding the additional impact of A0) in the coming year is £24.0m. The Mortgage Code Compliance Board (MCCB) regulated a larger industry; at its demise this comprised of around 10,000 firms and 38,000 registered sales staff at a cost of £4.4million per annum. This cost is less than the increase in actual costs required by FSA to cover the same, but significantly smaller sector, this year. FSA has a cost budget this year of £15.9 million for the intermediary mortgage sector. In the MCCB's five years of operation it issued 9,945 reports following visits to firms. In the interests of transparency, we are taking the opportunity of this consultation to request FSA to present similar statistics on its five years of regulating our sector.

The move to a straight line recovery model for fees, which disregards economies of scale, ignores the true risk profile of firms and with the network model in mortgages, will penalise severely a number of smaller firms who will suffer large increases due to the success of their parent organisation. There are many more appropriate risk indicators than firm size and we regret that a real opportunity to examine the true cost of regulating mortgage intermediaries has been lost. The fees being consulted on do not reflect the overall systemic risk that the sector poses to the economy. We would therefore urge FSA to revise their proposals.

## **Market Conditions**

We fail to see how such significant increases in the intermediary sector can ever be justified. Wider market conditions have resulted in the lending market having to restore a more responsible approach to lending, which in itself has resulted in reduced risk to consumers today. To then increase the fees of the intermediary community, who themselves were not at fault from irresponsibly lending practices of lenders, is simply unacceptable.

AMI continues to highlight economic conditions to FSA. With gross lending of approximately £144 bn in 2009, the conditions under which intermediaries operate – maintain competitive forces in the market – remain incredibly challenging. To increase the fees over by 32% is therefore unfounded.

## **Impact of A0**

AMI feels that the impact of the A0 class may also not have been fully acknowledged by the industry. Whilst the increase for firms with mortgage and general insurance permissions is small, the impact for those with just mortgage permissions is greater.

AMI also questions the policy intentions of the proposal. Under the revised structure, a mortgage firm without general insurance permissions could now apply for insurance permissions through notification and conduct up to £100,000 of business at no additional cost. It would not seem appropriate that the additional risk of a potentially inexperienced firm extending its permissions and conducting a significant amount of additional business would be represented by a zero increase in fees.

We also highlight the impact of A0 on the levy expense cost of other FSMA bodies such as FOS and FSCS. This exposure will result in AMI members bearing a further disproportionate increase, in addition to the 32% over fee rise, too.

## **Mortgage Intermediaries as a social good**

If the intermediary sector did not exist, or was not regulated, 'costs' would still exist because the products AMI members recommend would still be there and would present risk. In our view, a prime role of mortgage intermediaries is to maintain competition in the market. The market would not function as well without them and to this end, they are a social 'good'; consumers benefit from their advice and providers' distribution routes are kept clear, well maintained and cost effective. Consumers benefit from the holistic advice they receive from a whole of market adviser; not just the sale of a product.

We do share FSA's view that it is appropriate for Banks to subsidise the cost of regulating Credit Unions because of the social good they provide. Banks are happy to do this because they can see how the function of Credit Unions assists their own role on the high street. We would add, though, that mortgage intermediaries are also a force for good and that this should be reflected in the level of fees they are asked to pay.

## **Economies of scale**

The thrust of the modern financial services marketplace is towards cost-efficiency and economy of scale. Regulation and increasing levels of customer awareness have led to significant reductions in charges and profit margins on each product and this has been to the benefit of consumers. The inefficient practices and procedures of yesteryear were masked by higher charges on products and we welcome the fact that this situation is no longer tolerated.

These external pressures on the industry have also led to more focus on value for money and higher standards of customer service. Today's consumer has high expectations and is willing and able to complain if they do not receive what was promised or what they felt it was reasonable to expect. The industry is more flexible, innovative and customer-focused than ever before and this is good news for all concerned.

The reality of the increasingly efficient market that regulation has helped bring about should therefore be mirrored in the cost of its regulation. The move to straight line recovery we believe risks diminishing firms' potential to bring about ever-greater efficiencies and build on those that regulation and consumer pressure have helped bring about. Although this is a 2 and not a 3-star CP, consumers would inevitably suffer should some of the most efficient firms be forced to try to maintain current levels of service within more straitened circumstances.

We would urge FSA to consider risk metrics other than size. The evidence of economies of scale can be seen in the on-line library of historic data on firms and

sectors that has been collected via electronic returns. FSA should focus on the areas where the risks actually are until the benefits of the enhanced supervision programme are embedded and tangible. The assumption that all firms of the same size within a fee-block take up the same level of resource and present an identical risk is misplaced and could impact adversely, albeit unwittingly, on consumer outcomes.

## **Budget Process**

The budget process within FSA is not subject to a formal cost / benefit analysis. Rather a “top level” review is conducted in accordance with the Better Regulation Principles. However, we do not believe this to be sufficient for a budget now approaching half-a-billion pounds. In order to protect FSA from external criticism, reassure the firms who finance the regulator, and provide market confidence, we would support moves by FSA to adopt voluntarily a cost / benefit process in determining its budget.

It is now time for FSA, in conjunction with colleagues from H M Treasury to invite the National Audit Office (NAO) to review its budgetary process and conduct a value for money assessment on a regular, scheduled basis. This will provide FSA with confidence that its procedures are robust and also allow the regulator to answer any critics who worry about the closed book nature of the budget process. Further, FSA should discuss with H M Treasury if the Treasury Select Committee or the Public Accounts Committee is the better body to review the financial management of FSA. We would expect a consultation process for this move.

## **Compatibility**

FSA rules relating to fees are excluded from the statutory requirement to conduct a Cost Benefit Analysis (CBA). We are nevertheless concerned that regulatory action is being considered without clear market failure having been identified; we do not believe that the onus should be on the industry to prove the *absence* of market failure. Annex 1 (para 14) refers to larger firms having a greater impact on FSA’s statutory objectives. We cannot agree that size of firm is inevitably a more risky enterprise within the A18 fee-block which does not share the same capacity for systemic risk as the banks in the A1 fee-block. In setting a fees policy, FSA should not ignore the significance of sector, before firm size, as specific sectors and models within sectors have been the cause of real detriment in recent years.

AMI members and their clients are victims of the banking crisis; we would support whatever steps FSA deems it appropriate to take in order to mitigate the risk of reoccurrence. Our concern is the mapping across to other sectors, policy changes designed to fix problems with banks in the A1 sector.

## Questions

**Q1: Do you have any comments on the proposed 2010/11 FSA fee rates for authorised firms and the premium applied to the rates in A1 (deposit acceptors fee-block)?**

No

**Q2: Do you agree with the proposal to treat smaller non-directive friendly societies as an exception allowing them to pay a reduced minimum fee and the unrecovered minimum regulatory costs be applied to A.4 (insurers – life) fee-block**

No

**Q3: Do you have any comments on the proposed 2010/11 FSA fee rates for fee-payers other than authorised firms?**

Our concern is that fee-payers other than authorised firms meet the cost of their own regulation.

**Q4: Do you agree with the proposed change to FEES 3, Annex 5, Part 2, Category 2 to reduce the fee for vetting equity registration documents to £3,520?**

No comment

**Q5: Do you support our proposals for the new FEES 7 chapter?**

We fully support the principle of financial education and welcome the opportunity to discuss whether a new FEES chapter is the right way to meet the desired outcome of a better financially-educated populace.

As the Financial Services Bill has been passed by Parliament and a new Consumer Financial Education Body (CEFB) is established by FSA. Although this CP is concerned with that part of the CFEB's annual budget that is funded by 'fees raised from firms authorised under FSMA' it is important to consider proportionality; the proportion paid by authorised firms compared with

- "Public funds and dormant accounts, and
- Relevant consumer credit firms through the levies they pay to the OFT"

is a sensitive issue, particularly as the regulatory burden on firms is now higher than it has ever been and that firms are operating in economically difficult times. The CP refers to FSA contributing £32.9 million to the Financial Capability 2010/11 budget of £45.4 million but it is more correct to say that FSA *authorised firms* are making this contribution. 72% is a significant contribution by the industry. We therefore think it appropriate that CFEB's annual budget is subject to scrutiny discrete from the FSA approval that will be needed. We would like the scrutiny process to involve representatives of A-block fee-payers as the sign-off process as proposed is too remote from those who will actually have to pay the levies.

Consumers who use mortgage intermediaries do receive a measure of financial education via their relationships with them. Mortgage intermediaries are also making a significant contribution to financial education through pro bono work with the general public as well as with their own client banks. For these reasons, their contribution to the Financial Capability programme must be proportionate and bear in mind the role they are currently playing in improving consumer outcomes.

The success or otherwise of CFEB will be difficult to measure but, nevertheless, it must be an accountable body and demonstrate value-for-money. We would like to know, therefore, how CFEB's objectives are to be measured and in particular the obligation in FEES 7.1.3 G to enhance

- “The understanding and knowledge of members of the public of financial matters (including the UK financial system); and
- The ability of members of the public to manage their own financial affairs.”  
(*i.e., live within their means*).

These are noble intentions which we do support, but if money is being levied, they must be more than this; there must be measurable objectives and this involves setting out clearly how CFEB's success will be identified and measured. CFEB must be accountable to those who fund it if it is to have credibility.

FEES 7 may be a step towards meeting CFEB's objectives, but it should be kept under review. Its application should be proportionate as should the contributions made by all its 'sponsors'.

#### **Q6: Do you agree with our proposed £10 minimum levy for financial capability work/Consumer Finance Education Body?**

Our concern is with the overall cost of regulation for our members rather than the allocation of levies to the various activity groups. The notional £10 minimum levy should be spread across a wider range of band widths until the CFEB is up and

running and fee-payers know what *activities* are being funded and how these are being costed. The lack of tapering is unfair and punitive; we wish to see this revised.

**Q7: Do you agree with our proposed levies on periodic fees to recover the costs of financial capability work/Consumer Finance Education Body?**

No. The overall burden of regulation is increasing exponentially and FSA cannot expect industry to bear above inflation linked increases.

**Q8: Do you agree that we should apply to CFEB the same discounts that we apply to FSA fees, apart from the discounts on financial penalties?**

Yes.

**Q9: Do you agree with the changes we are proposing to the way the IMAP SPF will be charged in 2010/11?**

No comment.

**Q10: Do you have any comments on the proposed non-IMAP SPF for the period 2010/11?**

No comment.

**Q11: Do you agree that our proposed amendment to FEES4 Annex 2 Part 5 reflects the criteria set out in paragraph 9.23 of this CP and the requirements of the Solvency II Directive?**

No comment.

**Q12: Do you agree with our proposal to reduce the discount offered on the variable periodic fees charged to inward-passporting EEA and Treaty firms in fee-block A.1 from 80% to 50%?**

Our concern is that the cost of regulating these firms is met by them and reflects the full cost of FSA's work.

**Q13: Do you agree with our proposal to reduce the discount offered on the variable periodic fees charged to inward-passporting EEA and Treaty firms in fee-block A.3 from 100% to 90%?**

Our concern is that the cost of regulating these firms is met by them and reflects the full cost of FSA's work.

**Q14: Do you agree with our proposal to offer a discount of 40% on the**

**variable periodic fees charged to inward-passporting EEA fee-paying payment institutions in fee-blocks G.2 and G.3?**

Our concern is that the full cost of regulating the COB of all passported-in payment institutions providing payment services in the UK is met by those firms in full.

**Q15: Do you agree that the amendments we propose to insert into FEES 4 Annex 9 make our definition of the tariff base clear and unambiguous?**

No comment.

**Q16: Do you agree with our proposed glossary definition of securities derivative?**

No comment.

**Q17: Do you agree with our proposals for recovering the costs of setting up the regulatory regime for reclaim funds?**

No comment.

**Q18: Do you have any comments on the proposed 2010/11 FSCS management expenses levy limit figure?**

Please see our earlier response to this question.

**Q19: Do you have any comments on the proposed 2010/11 FOS general levy rates?**

We are pleased to see that the percentage of FOS's total funding raised via case fees is on the increase, thus reducing the amount raised by levy. Applying the greater share of cost to those firms that pay case fees is a fairer method of funding the industry-wide service.

The number of complaints against mortgage intermediaries remains very low and we acknowledge that there is a freeze on the flat fee levy for industry block 16 as well as the case fee. This is welcome news at a time when the overall cost of regulation is on the increase.

Retaining the number of free cases at three for each firm is also positive; this effectively means that the vast majority of AMI members will not incur case fees at all as, on the whole, they receive very few complaints.