



Association of Mortgage Intermediaries response to FSA's CP11/31 Mortgage Market Review: Proposed Package of reforms

Introduction

This response is submitted on behalf of the Association of Mortgage Intermediaries (AMI). AMI is the trade association representing over 80% 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.

AMI welcomes the opportunity to respond to FSA's latest consultation paper on the Mortgage Market Review (MMR).

Background

We welcome that FSA continues to consult openly and constructively with the mortgage industry. However, this response is based on the whole consultation as presented in this paper. If further changes are made to aspects of the proposals at a later date then it is highly likely that this would impact on our view of other areas of the MMR consultation. In particular, if there are changes to the proposed binary world of advice and execution only, then this is likely to have significant impacts on other aspects that would materially alter our response.

As AMI has argued throughout the MMR process, the issues arising in the UK mortgage market in the 2005 to 2008 period were capable of having been dealt with by proper application of MCOB and the supporting rules, principles and statute, through effective FSA supervision.

The recent confirmation of this at the Treasury Select Committee by the FSA Chairman and Managing Director, leave us in a difficult position. We have long supported the principles and aims of MMR, but been vigorous in arguing that it should not be too extreme or stifle innovation, choice and the ability to get on the housing ladder. We consider it essential that the particular risks are clearly set out to provide the correct context and detail. Accordingly, in the final Policy Statement and final rules we would like to see a clear analysis of the agreed risks and issues, with the consequent delivery of effective and proportionate changes to the principles, rules and guidance.

Whilst these most recent proposals remove many of what we previously considered the more extreme and restrictive aspects of the proposals, the remaining consultation still introduces extreme difficulties for lenders, brokers and consumers. The need to ensure we do not damage the market for such as the self-employed, those on interest only loans or the credit impaired is crucial. Rules which impose significant detail in some areas but leave lender's discretion in higher risk areas is liable to lead them to avoid operating in such sectors.

This is a complex set of inter-related proposals, which the FSA has acknowledged, so we remain concerned at the scale and tone of the changes still being recommended. The inter-connectivity of the proposed changes makes it likely that we will see market participants react differently to the changes and there is the risk of over-reaction. We would like the new FCA, to monitor carefully all implementation to avoid the risk of unintended interpretations and consequences.

In addition, in such a restricted economy as we have today, we are concerned that the proposals may further reduce the number of lenders and competition in an already difficult market. The risk that the proposals might lead to dominance for a few players has not been adequately addressed. With only 6 lenders of scale who also dominate the current account market, any move which reduces competition needs to be carefully considered. The vibrant broker market delivers competitive edge, and any regulation that might reduce this, risks creating poor consumer outcomes.

Some have argued that the proposals are a "vanilla, one-size-fits-all" approach. Indeed we consider that some of the proposed rules move towards mortgages only being available to PAYE tax paying, UK citizens with existing equity. There are risks for lenders in opening up loans to other groups as it will be harder to evidence affordability. The intermediary sector is concerned about the unintended consequences of the proposals.

Executive summary

- We are fully supportive of the proposals to make advice the default position for all mortgage transactions, with an execution-only opt out for those consumers who are aware of the product they want and the protections they are giving up. We believe that this division provides clarity to both consumers and industry.

- We support the recommendations to make lenders responsible for assessing affordability, but are concerned that the ability to delegate certain tasks will not occur due to the specific responsibilities placed on lenders in the draft rules.
- We consider that in isolation the proposals appear sensible. However, considering how all the combined factors work together, in practice, will be essential for ensuring that the MMR can be implemented successfully. We believe that, in combination, the proposals may limit lenders propensity to delegate and to lend. The combining of the various parts of lender's responsibilities risks encouraging them to migrate all risks in house, to attain appropriate oversight and control.
- We are particularly concerned about the interest-only and transitional arrangements proposals. Whilst these are welcome developments, they need to be expanded upon to provide appropriate consumer access. We believe that some additional borrowing should be allowed, within controlled amounts, and monthly repayment costs should also be allowed to increase, where this is in the customer's best interest.
- We strongly believe that any changes to the interest-only rules should not be applied retrospectively. Our support of any MMR proposal is reliant on them not being applied retrospectively by either FSA or by FOS.
- We also have some concerns over the how the policy intention is transmitted into the draft rules and how FSA's supervision teams are treating these proposals, which are still under consultation.
- The expansion of the approved persons' regime to the mortgage industry is a core part of the MMR proposals. We are extremely disappointed to see that the application of individual registration has been delayed indefinitely. We call on upon FSA to reconsider the decision to delay the implementation of individual registration. The benefits that individual registration will provide to the industry and to consumers are too important to be delayed any further.
- We support the reduction in the level of paperwork that a consumer must receive as part of the disclosure provisions.
- We believe that with the move to make advice the norm, the introduction of the customer best interest provision and the enhanced affordability provisions, more latitude can be given in the transitional arrangements and there is limited need for the high risk categories suggested.
- Whilst supportive of the desire to provide exemptions for professionals and high net worth consumers, we do not consider main-stream lenders will develop such strategies for the limited number of such applicants. Total exemption for high net worth targeted lenders is our preferred route.
- FSA is right not to apply RDR style scope of service labels to the Mortgage Market. We support this proposal as this will allow for a sensible plain English statement covering what the adviser offers.

Key issues

Advice

The FSA proposal to make advice the default position for all mortgage transactions is a major transformation for the mortgage market. The majority of mortgage intermediaries already operate a fully advised model, so they will see less of a change compared to most mortgage lenders and their direct sales forces, which have generally traditionally operated in a non-advised remit. This is the bedrock of the new proposals and will serve to deliver improved outcomes for all consumers.

Mortgages are typically the largest transaction a consumer undertakes, and it is generally accepted that there has been evidence of consumer confusion between advice and guidance (non-advised). Therefore, the proposal to make advice mandatory is welcomed.

These changes could have an impact on the way distribution within the mortgage market operates. Lenders may adapt their business models to focus more on intermediary distribution or move further (or completely) to a direct distribution model. Whilst these are both risk based and commercial decisions for firms to consider, FSA must not underestimate the long-term impact of these changes on the market and consumers.

Lenders will see pressures on their business models as a result of these changes. The removal of the non-advised sales process will impact on the way in which lenders have traditionally dealt with back office issues. However, these issues should not diminish from the objectives that FSA is trying to achieve. Lenders will have to adapt but the changes made under the proposal will result in improved outcomes for consumers. We believe that on balance these changes are justified. Some will argue that putting all consumers through an advice process will unduly lengthen the process for many. However, when we have gone through lender based non-advised processes, these are little different in time and complexity from an advised interview. The detail required to make a mortgage application or satisfy an existing lender under current criteria, when completing any application today, is very similar.

FSA has set out what constitutes an advised sale process and has specified what consumers need to know to obtain a mortgage on an execution-only basis. However, this leaves the question of how lenders transact with their customers during the term of the mortgage.

We are aware that lenders currently and historically have used the non-advised provisions in MCOB to undertake 'transactional' tasks, such as converting a customer from interest only to capital repayment, extend or shorten the term. However, more fundamentally, this has also included agreeing retention deals. This could involve proceeding with a further fixed rate deal or moving to a tracker, which does not, in the lenders' eyes, vary the mortgage contract. Currently staff who undertake these arrangements do not

need to be CEMAP/MAQ qualified, nor are they subject to on-going training and competence requirements.

It would seem unlikely that these tasks could be undertaken on an "execution only" basis as the customer will generally arrive with a problem, and the lender representative provides a solution usually through verbal interaction. Under the FSA's advice proposals this interaction must be considered to be advice.

Furthermore, in making these changes a lender may be varying a fundamental part of the advice provided by an intermediary on the appropriate product based on the consumer's needs and circumstances. If the lender varies the product and therefore the advice, surely this then means that the lender is taking on that responsibility. It would seem logical that any FOS rights would then be taken over by the lender or, if not, that it must be acknowledged that the consumer is losing their FOS rights in relation to the original advice.

There appears to be some calls from lenders for a 3rd way. This would mean not only the binary world of advised and execution-only, but also a means of incorporating "transacting". If this were not the intention of FSA then this should be made clear. If it were the intention of the consultation to have this approach, then the rules as drafted do not make this apparent.

We would be concerned if these unqualified "transactors" are allowed to, for example, recommend a new fixed rate and consolidate the fee into the loan. Given the new MMR proposals on how adding fees to the loan must be addressed in an advised sale, it seems illogical to allow this to be repeated on a number of occasions during the rest of the life of the loan without proper explanation and advice.

It is difficult to see how such an activity is not captured within the new advice framework if a logical and consistent approach is adopted and one that provides a level playing field. Accordingly AMI supports this binary approach of advice or execution-only continuing and being implemented by the FSA.

Evidencing income

FSA's view is that it was always its intention under MCOB that the lender should be accountable for its decision to lend. We would be surprised if any lender's shareholders thought that this was not the case. FSA has proposed to tighten its rules by making the lender fully responsible for the affordability assessment. AMI supports this change.

Part of these proposals would require that the lender obtains evidence of income but this can be outsourced to a third party. However, FSA must ensure that the rules reflect this policy intention and that FSA's supervision team understands the capacity for lenders to do this. Ultimately it will be the lender's decision as to how and to whom these processes and others are outsourced. But the rules must allow for this flexibility to be available whilst lenders retain the regulatory responsibility. We are concerned that the weight

of the rules and guidance includes such detailed provision that will prevent the lenders from undertaking this in practice.

Interest-only proposals

FSA's position that a repayment mortgage is generally the logical starting point for most consumers is a sensible one. However, this should not be at the expense of accepting that for a significant minority of consumers an interest-only mortgage will be the most appropriate method of borrowing for their specific needs and circumstances.

There are some consumers, but certainly not all, for whom interest-only may be a better alternative to renting. For example, a property purchased using an interest-only mortgage could allow the consumer to build up some level of equity over the lifetime on the loan. This increase in equity would not necessarily remove the need for a repayment strategy, but the concept of property price inflation cannot be wholly ignored.

Unlike rental payments, the payments on an interest-only mortgage are not subject to inflationary increase over time. For example, a consumer can benefit from using a fixed rate mortgage to provide security over a large part of their expenditure, which could not be provided for someone in rental accommodation.

In addition, property ownership provides a level of security of tenure that is unparalleled in renting. This is partly driven by assured short-term tenancy agreements and buy-to-let mortgages often not allowing for tenancy agreements of more than 1 year and many for not more than 6 months. Therefore, property ownership could provide a family with the security of tenure needed to ensure that their children are able to attend their preferred local school, without the concern of being forced to move on once their tenancy agreement expires.

We are concerned about the use of some terms around the type of repayment strategy that can be used. FSA suggests that a 'speculative' repayment strategy will not be acceptable. It is our understanding that, by this, FSA means uncertain outcomes, such as potential inheritances that the consumer expects to receive. However, using the term 'speculative' without further clarity within the draft rules has been interpreted by some to include equity based investment vehicles.

We do not believe that it is FSA's intention to exclude these types of investment products, or the potential for growth in their capital values, from being used to repay an interest-only mortgage. However, it does demonstrate the concerns we have on how such proposals will be viewed, in particular in the context of the disconnect between policy intention, rules and supervision.

We strongly believe that any changes to the interest-only rules should not be applied retrospectively. Our support of any MMR proposal is reliant on them not being applied retrospectively by either FSA or by FOS.

We support the MMR interest-only proposals being flexible to allow lenders to set their own risk tolerances. FSA has set parameters around the use of sale of the property as a repayment method. However, there may still be a need to provide flexibility to take account of regional price variations and consumers changing needs and circumstances over time. Not allowing such methods could hold back mortgage transactions and innovation within the market.

The ability for the lenders to consider whether a repayment strategy is credible must not be considered as a de-facto guarantee that the strategy will repay the outstanding capital at the end of the term. As with a capital and interest mortgage, the consumers must be ultimately responsible for the repayment of their mortgage debt.

An issue that FSA does not address is what would happen if the repayment strategy is no longer considered as a credible strategy to repay the mortgage debt at the end of the term. We believe that this is an important part of each lender's lending policy. The lender must be free to establish its own policy and procedures for addressing this issue, such as migrating some of the loan to capital and interest. In addition, property sale must be seen as credible from a policy perspective, provided the "outcome" is understood by the customer. At the same time, the right to vary terms must clearly be fair and FSA has reminded lenders of this in the very recent past.

Transitional arrangements

The transitional arrangements will need to protect consumers who have taken out a mortgage prior to MMR proposals coming into force. It will also need to ensure lenders honour the customers original contract terms. In particular, where the lenders own lending criteria has altered, due either to regulatory change or to the lender's own circumstances, but the consumer's circumstances are the same, the consumer should not be disadvantaged.

The transitional arrangements should aim to reduce the impact on consumers who could otherwise become property and/or mortgage prisoners. This is particularly the case for those who may have self-certified in the past, have good payment histories and have enjoyed the benefits of interest only loans. It is important that the market continues to allow such existing customers to have some flexibility, without taking on significantly greater financial exposure.

For example their property may now be unsuitable because the family is growing in size and a larger property is now required to the one that was obtained under the pre-MMR contract. Equally a consumer may now want to downsize because they no longer require the size of property they purchased via a pre-MMR mortgage contract.

We are concerned that the proposed transitional arrangements will not produce the desired outcome unless they are enhanced. FSA has rightly identified that there is a clear need for some form of transitional arrangements to be in place to ensure consumers are not substantially dis-advantaged, trapped or become mortgage prisoners. Avoiding such consumer detriment is

key. For example, if a consumer wants to change to a fixed rate mortgage to ensure a greater degree of certainty about their expenditure, even if it means an increase to their monthly repayments, it may be in their best interests to do so. Through the MMR advice and the customer's best interests' proposals, the regime should give comfort that good outcomes in these circumstances are achieved.

In addition, there may need to be a greater degree of flexibility on the "no new borrowing" restriction. There may be certain circumstances where a small amount of additional borrowing may be in the consumer's best interests, or may even be needed to make the move viable i.e. to cover stamp duty, estate agents and removal costs etc. Such flexibility should be left for the lender to determine as part of its lending policy but we would consider a 10% tolerance on both the additional borrowing and the monthly cost of borrowing to be a reasonable amount.

These amendments are required to maintain a degree of social mobility, protect a flexible labour market in the UK and to ensure that any suppression of normal market volumes does impact the wider economy. Failure to allow flexibility in this area will potentially stifle transactions in the house purchase market and also result in many existing borrowers being left unable to re-mortgage elsewhere to get a better rate due to them not having cash set aside to cover any fees.

Extending the current Approved persons regime to cover the mortgage industry

When the FSA took responsibility for the regulation of the mortgage market, from the Mortgage Code Compliance Board, the industry's biggest concern was the loss of the Code's register of "members".

Despite strong industry lobbying FSA deemed it to be overly bureaucratic and it was not transferred. Thus as the market expanded from 2004 it lacked these additional controls and tracking tools. The re-introduction of an authorisation and registration process was called for by the industry, agreed by the consumer lobby as essential and promised by the FSA's Mortgage Market Review in Policy Statement PS 10/9 dated June 2010.

The announcement recently, by an amendment on FSA's website, of an indefinite delay to any process again limits the ability of the industry to drive out those who seek to damage consumers and firms. This is despite the fact that the levies on the industry increased significantly to cover the MMR work including registration.

There is much to be done to improve consumers' perception of the industry. A robust authorisation and registration scheme which can identify and isolate rogues would improve this. As a means of combating fraud and ensuring consumers are aware of those who are authorised, this is an essential core tool. We consider that FSA should find the resources to implement this enhancement as a matter of urgency.

Disclosure labels in the mortgage market

FSA has proposed not to adopt the RDR style disclosure labels of 'independent' and 'restricted' to the mortgage market as they do not believe they are adequate reflections of the make-up of the prevailing business models. This recognition of the limitation of such labels is welcomed. FSA's mortgage policy team have shown substantial awareness of the way the market operates. We support the latest MMR recommendations in this area.

Equity release

The majority of Equity Release plans involve the roll up of interest. However, there is one current plan which allows the customer to make monthly interest payments. In such circumstances, if the customer fails to make the monthly interest payments, the plan automatically reverts to a roll up of interest scheme. One of the reasons customers opt for this type of interest only Equity Release plan compared to a traditional interest only mortgage, is because they are aware that they have the safeguard of the plan reverting to a roll up of interest in the event of any payment difficulties. Given this, in such circumstances, we believe Equity Release plans should be exempt from the income, expenditure and affordability requirements given that the terms and conditions of the plan confirm the automatic transfer of the plan to roll-up of interest basis in the event of default on the monthly interest payments. Therefore, there is no risk of any customer detriment.

FSA's consultation on MMR

Throughout the MMR consultation process the FSA Mortgage Policy team has engaged well with the industry. Where the proposals would have a significant adverse effect on the market, these have been taken into account, without this having an adverse impact when measured against enhanced consumer protection or benefits.

The progression throughout the consultation process has resulted in the current range of proposals being much more proportionate and aligned with both the interests of consumers and a robust and responsible mortgage market.

Future changes to the MMR consultation

FSA latest consultation paper has provided feedback and reconsidered the previous two papers in one combined document. FSA has in effect acknowledged that its proposals for the mortgage market are interconnected. Therefore, it is important not to consider individual sections or proposals in isolation. If FSA does go back and make significant changes to parts of its proposals it must also reconsider how this impacts on the MMR as a whole. For example, changes to the advice proposal, could impact on a range of proposals covering approved persons, qualifications, disclosure requirements and the way appropriateness is assessed. Significant changes to

components should require further consultation to avoid the risk of consumer or market detriment and unforeseen consequences.

Disconnect between FSA policy and supervision

FSA needs to consider how its rules are interpreted by their supervisors as we believe these sometimes differ from the original policy intention.

FSA also needs to be more aware of any disconnect between its policy intention in these proposals and how supervisors might encourage firms to introduce those proposals before they have even become rules.

In introducing new minimum standards there are a range of firms who will wish to comfortably exceed these in order to ensure regulatory certainty. This is liable to lead to 'best practice' being above the levels seen in these proposals and therefore a further ratcheting up of standards, with the risk this could reduce choice for consumers.

In order to allow sufficient time for the industry to become ready, some elements may need up to 18 months deferment from the publication of final rules.

European Mortgage Directive

AMI remains concerned that these proposals may not harmonise perfectly with the proposed EU Directive. We are concerned that the sensible reduced disclosure provisions in MMR could be superseded by a directive.

In addition, the draft Directive indicates that fees may not be taken in areas where advice is compulsory. Our concern is that it is rightly FSA's intention to ensure that certain consumers who are pursuing high risk outcomes need advice. The EU provision is to prevent vulnerable consumers being charged excessive fees. However we need to ensure that advisers can still be paid reasonably for the work in areas of compulsory advice, as it is essential that these groups benefit from an adviser acting in their best interests.

Conclusion

We are broadly supportive of this latest set of proposals subject to the concerns expressed in this response.

Consultation questions

Chapter 1

No questions

Chapter 2

No questions

Chapter 3

Q1: Do you agree that lenders should detail how they incorporate anti fraud controls into their affordability assessments in their responsible lending policy?

Consideration will need to be given to the level of information that is provided. Clearly lenders will be concerned about providing information that could be potentially exploited by fraudsters. However, this is not a justification for not providing any level of information about lender's anti-fraud controls.

Q2: Do you have any comments on our income proposals?

Lenders should be ultimately responsible for the funds they lend. Mortgage intermediaries will clearly still want to consider their clients' income and expenditure as part of the advice process to ensure that their recommendation is suitable, even if their regulatory responsibility for assessing income only extends to considering whether the income meets the lender's mortgage criteria.

Q3: Do you agree with this approach to expenditure? Do you have any comments on the categories of expenditure? Do you have any practical concerns about implementing this approach?

The three categories of expenditure are sensible and it is certainly a more workable approach than the previously proposed 'free disposable income' method. However, it is important to remember that circumstances will vary between consumers. A one size fits all approach would not be appropriate. Some items of expenditure which may be seen as essential for one consumer may not be for another. What is considered to be basic quality of living costs by one person may not be by another.

It would seem likely that most lenders could use credit reference agencies to consider and check committed expenditure. For basic essential expenditure and basic quality of living cost the Office of National Statistics (ONS) information would be the most logical source for consideration and checking. However, some level of flexibility is essential to take account of the consumer's actual circumstances.

We are concerned that allowing lenders to use their own data, including credit scoring, from consumers' current accounts could create an unfair competitive

advantage. There has been substantial consolidation in the banking sector since the start of the financial crisis. The majority of consumers will hold current accounts across a small number of banking groups which also operate mortgage lenders. This level of consolidation would not have been acceptable on competition grounds under normal market conditions. Banking groups such as Lloyds Banking Group have not yet pared back their branches and continue to benefit from their artificial position. MMR must not put rules in place that allow lenders to substantially benefit from this position.

We do not consider that the competition issues have been adequately addressed within this paper and we remain concerned over the dominant position of some large lenders who also hold a significant proportion of current accounts.

Q4: Do you have any comments on our proposed approach to assessing affordability against future interest rate increases?

Historically predictions on interest rates changes over the medium term have been poor, from even the most highly regarded sources. In 2008 would anyone have predicted that Bank of England base rate would have remained set at 0.5%, for over three years, from 2009 through into 2012? We are concerned that predictions will need to be made for up to 5 years. We are not sure how realistic it is to expect this to be done with the level of accuracy FSA models would appear to require.

What will be the implications on both lender and advisers if a consumer is recommended a mortgage where the future rate increase stress test proves to be insufficient? Are lenders to be held accountable for the accuracy of their selected rates? FSA should provide clarity on this issue.

Q5: Do you agree with our assumption that 90% of lenders already apply a stress-test?

This is a lender issue

Q6: Do you think that lenders are currently applying a stress test of a similar degree to the test we propose?

This is a lender issue

Q7: Do you have any comments on our proposal to drop the requirement that affordability should be assessed on a maximum term of 25 years?

We support the removal of the proposal that affordability must be assessed over a 25 year maximum term. Such proposals would not allow consumers, who did not meet the 25 year requirement, to have a mortgage over a longer term even if it was perfectly affordable and reasonable for them to do so.

Furthermore, consumers' needs and circumstances can be more complex than requiring a simple 25 year term mortgage. The state retirement age will be removed and state pension age is rising. To put in place a set term for

mortgages to be assessed, would suppress mortgage transaction and innovation in the market, without obtaining increased consumer protections for all of those excluded under such requirements.

Q8: Do you have any comments on our proposals to protect credit-impaired consumers?

We would agree that a greater level of care will need to be provided for such consumers. Much of the necessary protections will be applied under the increased affordability assessment proposals.

Making advice mandatory for debt consolidation is logical step to help ensure that these vulnerable consumers are sufficiently protected.

FSA has suggested two alternative approaches to this issue.

11.6.14 R

(1) This *rule* applies where:

(a) a purpose of a *regulated mortgage contract, home purchase plan* or further advance is debt consolidation; and

(b) the *customer* is a *credit-impaired customer*.

[(2) *Option 1* Where each of the conditions in (1) is satisfied and, if the debts which are to be repaid using the sums raised by the *regulated mortgage contract, home purchase plan* or further advance were not repaid, the transaction would not be affordable for the *customer*, the *firm* must take reasonable steps to ensure that, on completion of the transaction, those debts are actually repaid.]

[(2) *Option 2* Where each of the conditions in (1) is satisfied, the *firm* must assume that the *customer's* existing debts which are to be repaid using the sums raised by the *regulated mortgage contract, home purchase plan* or further advance will not in fact be repaid and, accordingly, include them as committed expenditure in the affordability assessment for the *customer*.]

Our concern is that option 2 is not viable alternative. The reason most consumers would want to consolidate debts would be to reduce total expenditure. If the re-mortgage assessment is based on this expenditure being retained within the assessment, then this will result in many mortgages being declined on the basis of an affordability assessment that is not representative of the on-going reality.

This outcome would be counter-productive as it would stop many consumers from being able to effectively and proactively manage their financial commitments.

Option 2 is the more likely of the two to restrict consumer access and reduce transactions. Option 1 will increase administration in lenders but the process described in option 1 has already been used by some sub-prime lenders. As such we would support option 1 over option 2.

Regardless of what option is adopted it is important that it is only applied when the FSA definition of credit-impaired is met, not the lenders own interpretation or definition.

Q9: Do you think that our proposed enhanced sales standards will provide adequate protection for right-to-buy consumers? Are further measures required?

We agree that right-to-buy (RTB) should be considered within the vulnerable consumers categories and that advice should be mandatory for these consumers. Many of the new affordability proposals should provide substantial additional protections for these consumers.

It is also important to remember that there are additional factors that will also need to be considered for RTB transactions, such as the impact on welfare benefits, future leasehold costs and the limitations on reselling the property.

The Department for Communities and Local Government (DCLG) has consulted on the government's plans to expand the Right-to-buy scheme. The protections required for RTB consumers go beyond those that are regulated by FSA. FSA will need to be mindful of these developments.

Q10: Do you think income multiples could work under our proposed rules? If not, why?

The majority of lenders have moved away from relying on income multiples to using more sophisticated assessment methods. Only smaller lenders, such as small building societies, have retained income multiples as their primary assessment method.

Lenders can still apply income multiples as part of their lending policy. However, this should not remove their requirement to conduct an assessment of a consumer's income and expenditure. To ensure consumer protection we would support a level playing field across all lenders. We do not believe that consumer protections should vary between lenders.

Q11: Do you have any comments on our proposal to require lenders to take into account information about future changes to income and expenditure?

Current draft rules provide a sensible limit on the extent to which future changes can be foreseeable.

11.6.13 G

(1) Examples of future changes to income and expenditure in *MCOB* 11.6.12R are: reductions in income that may come about following the *customer's* retirement; where it is known that the *customer* is being made redundant; or where the *firm* is aware of another loan commitment that will become due during the term of the *regulated mortgage contract* or *home purchase plan*, such as an equity loan to assist in property purchase.

We would not support any extension to this guidance to cover changes that go beyond what is reasonably foreseeable.

We are concerned about what questions intermediaries will need to ask to satisfy their understanding of future changes in circumstances and how they sit with in the current gender discrimination legislation. For example, how far can or should an adviser question applicants on their future plans for children.

Q12: Do you agree, that to ensure these proposals work, we should define a credit-impaired consumer? Do you agree with our proposed definition?

For the proposals to work a clear definition of credit-impaired is required. We would support the proposed definition. However, clarity may need to be given to the fact that those not meeting the definition are not necessarily considered as free from impairment. It should be up to lenders to set their own parameters around such lending/product criteria.

Q13: Which option do you prefer? Option 1, where the lender would be required to take reasonable steps to ensure that debts to be consolidated are repaid? Or option 2 where the lender would be required to assume that debts to be consolidated remain outstanding for purposes of assessing affordability? If you disagree with both options, what do you suggest as an alternative?

See question 8

Q14: Do you agree with our proposals to strengthen lender's systems and controls around responsible lending?

As part of the lender's systems and controls it should retain the ability for the lender to outsource income checking and other parts of the data capture and verification process to intermediaries.

We would agree that any decision to do so and any requirements around how this should be done should be clearly demonstrated in the lender's responsible lending policy.

FSA has stated that it does not want to prevent income verification being outsourced to an intermediary, providing that appropriate systems and controls in place. The draft rules state

11.6.7 G In relation to taking account of the *customer's* income for the purposes of its assessment of whether the *customer* will be able to pay the sums due:

(6) a *firm* may use information provided to it by a *home finance intermediary* or other third party, including electronic sources of information, but the *firm* will retain responsibility for compliance with this chapter; and

However, FSA must ensure that its other rules allow this to happen in practice. We are concerned that lenders' reading an interpretation of draft

rules 11.6.1.G and 11.6.2.R would remove any appetite for lenders to outsource to intermediaries. This would be a poor consequence of these changes.

Q15: Do you have any comments on our proposed transitional arrangements? Do you think they will be sufficient to address risks to consumers? Will they create any additional risks to consumers?

We are concerned that the proposed transition arrangements will not produce the desired outcome unless they are substantially enhanced. FSA has rightly identified that there is a clear need for some form of transitional arrangements. However, the proposals need to be expanded upon to make a significant difference to these consumers.

The transitional arrangements must not just be offered with the current lender. Such a potential lack of competition will drive poor outcomes for consumers. It is essential that the consumer has the ability to use these arrangements to change their mortgage lender. Lenders should not be able to artificially profit by their lending policies creating captive customers. For example a client who has legitimately been accepted under the mortgage lenders criteria, such as a self-certification borrower, but is now unable to obtain a new product from that lender, due to the changes in criteria rather than a change to the borrower's circumstances. FSA and lenders must be mindful of unfair variations of contract terms.

The transitional arrangement should be expanded so as to ensure that the consumer's best interests can be accounted for. Furthermore, they should only be conducted on a fully advised basis. There needs to be a degree of compulsion in all of this for lenders to utilise transitional provisions, as failure to do so would simply lead to profiteering from captive customers who have no option to move elsewhere – this cannot be in consumer's interests and as the Rules stand could be a very real unintended consequence.

Those consumers who can demonstrate a good repayment history with their current lender should be able to remortgage. This should only be for existing business. There is no additional risk for lenders as these clients are already in the lending system. Those consumers who do not have a good payment history will not qualify

If a consumer wants to change to a fixed rate mortgage to provide more certainty about their expenditure they should be able to do so, within parameters, even if their monthly repayments will increase, as it may be in their best interests to do so.

There may also be circumstances where a small increase should be allowed to the capital borrowed, to a maximum of 10% or a maximum additional £10,000. We would also consider a 10% tolerance on the monthly cost of borrowing to be a reasonable figure.

From a broader economic perspective, transitional arrangements will be essential as no one wants a stagnated market for this large group of

consumers. Labour mobility is essential to the economy and housing transactions create substantial economic benefits for the wider economy.

Clearly lenders will want some form of safe harbour from FSA for using the transitional arrangement. It is essential that FSA consider the interaction between how lenders apply the post MMR MCOB rules, under the transitional arrangements and those that fit within the exceptions process. This will not just be an issue for the rules, but also for FSA's supervision teams and consideration will need to be given to how FOS would consider such a process.

The advice proposals and the consumer best interests rule should result in good outcomes for these consumers. These transitional arrangements should be undertaken on a fully advised basis.

Q16: Do you think that there is sufficient protection for mortgage borrowers who are 'trapped' with their current lender? If not, what additional protection do you suggest?

Some borrowers are unable to obtain a new mortgage on today's terms. MMR will only increase this problem which is why it is essential that the transitional arrangements work in practice.

In addition there should be a greater focus on consumers being able to port their mortgages to new properties to increase the ease of labour mobility for those who are trapped with a lender or in a property that is no longer suitable. Whilst this is a commercial matter for lenders, FSA must still do more to ensure that lender facilitate consumer's needs. Emerging evidence in the market place is that this is not happening and that lenders are quite content to vary underwriting thresholds for existing customers which ultimately trap them where they are.

FSA should consider that these restrictive practices have already disadvantaged many consumers whose mortgages were securitised, or whose lender has ceased lending to new customers. MMR should not add to this problem.

Q17: Do you think the eligibility requirements are appropriate? Should we allow these transitional arrangements to be used where the new monthly payment is higher?

See question 16

Q18: Should we allow the transitional arrangements to be used where there is a material change to the mortgage, such as the removal of a borrower following a divorce? How could gaming be prevented?

This may not result in a material change to the mortgage contract. However, if it does then this should certainly allow transitional arrangements to be applied to benefit those 'trapped' consumers.

**Q19: Do you think these arrangements will be practical to implement?
How could they be improved or simplified?**

See question 16

**Q20: Do you agree that the draft rules on responsible lending in the draft
Mortgage Market Review (Conduct of Business) Instrument 2012, at
Appendix 1, reflect the stated policy intention?**

Amendments to the Glossary of definitions

bridging loan

a *regulated mortgage contract* which has a term of twelve *months* or less.

credit-impaired customer

a *customer* who:

- (a) within the last two years has owed overdue payments, in an amount equivalent to three *months* ' payments, on a mortgage or other loan (whether secured or unsecured), except where the amount overdue reached that level because of late payment caused by errors by a bank or other third party; or
- (b) has been the subject of one or more county court judgments, with a total value greater than £500, within the last three years; or
- (c) has been subject to an individual voluntary arrangement or bankruptcy order which was in force at any time within the last three years.

It is important to clarify that lenders are still able to set their own parameters around what they consider is a credit impaired consumer. Consumers who do not meet this definition should not automatically be considered to be non-credit impaired. We would be concerned about complaints arising where a consumer who does not meet FSA's credit-impaired definition, but still has some form of impairment, so does not qualify for a lender's prime product might take retrospective action on the basis that they were advised when their circumstances did not fit the definition.

direct deal

a *home finance transaction* that can only be obtained direct from a *home finance provider*, where that *home finance provider* is not the ~~selling~~ *advising firm*.

initial contact

the first occasion when a *firm* is in contact with the *customer* and may perform any of the following in relation to a *home finance transaction*:

- (a) *advising* on the transaction;
- (b) *arranging (bringing about)* the transaction; or
- (c) *entering into* the transaction, when there is no *firm arranging (bringing about)* the transaction.

Amendments to the Mortgages and Home Finance: Conduct of Business sourcebook (MCOB)

2.2 Communications

2.2.5 G *Firms* are reminded that they should follow the relevant *rules* in COBS 6 and COBS 13 relating to advice and disclosure on *investments* if they are *advising* the *customer* on an *investment* such as an annuity associated with an *equity release transaction* or an *ISA* used as a *repayment strategy*.

It is important to consider that whether or not regulated investment advice is provided, the consumer accepts ultimate responsibility for the repayment strategy meeting its objectives.

2.5A The customer's best interests

2.5A.1 R A *firm* must act honestly, fairly and professionally in accordance with the best interests of its *customer*.

It is important that this rule, when applied in conjunction with an advised sale, does not mean that the mortgage intermediary is, inadvertently, acting as an agent of the client. It is important that this clarity is provided in the rules.

4.4A Initial disclosure requirements

4.4A.10 G

(4) For face-to-face and telephone contact, a *firm* should comply by building the messages into the initial oral discussion with the *customer*.

We are concerned about how a smaller intermediary firm will adequately record that such disclosure has taken place. Large lenders may have call recording equipment but this is less common in smaller intermediaries and the cost of installing it would be disproportionate.

4.6A Rolling-up of fees or charges into loan

4.6A.1 R A *mortgage lender* may not offer a *regulated mortgage contract* to a *customer* on the basis that fees or charges of any kind (receivable either by the *mortgage lender* or another party) are automatically added to the sum advanced.

4.6A.2 R A *firm* must not undertake any action that commits a *customer* to an application for a *regulated mortgage contract* where a fee or charge of any kind (receivable either by the *firm* or another party) is to be added to the sum advanced under the *regulated mortgage contract*, unless the *customer* has made a positive choice to add the fee or charge to the sum advanced.

We would consider that this would mean that any even if the sale is a retention deal offered by the existing lender, then such a sale must still be conducted on a fully advised basis due to the interaction taking place around the positive election.

4.7A Advised sales

4.7A.1 G

(3) The *rules* at MCOB 4.8A also provide that *advice* must be given wherever the sales process involves spoken or other interactive dialogue (except for *high net worth customers* and *professional customers*) unless the *customer* elects not to receive *advice* and to proceed on an execution-only basis.

We consider any lender retention deals or changes to rate, term or method of repayment should also be caught by the requirement for the sale to be fully advised. Lenders should not be able to circumvent the advice rules under the guise of contract variations or transactions, if those actions would be considered as an advised sale if that consumer changed lender.

4.7A.9 R In relation to MCOB 4.7A.6R(2), where a *firm* has identified an *interest-only mortgage* as appropriate for a *customer*, the *firm* must ensure that the *customer* is aware that he will have to demonstrate to the *mortgage lender* that he has a clearly understood and credible *repayment strategy* in place, in order for the *mortgage lender* to be able to satisfy MCOB 11.6.24R(1).

4.7A.10 G MCOB 4.7A.9R does not require a *firm* to *advise* the *customer* on a credible *repayment strategy* or assess the adequacy of a *customer's* existing *repayment strategy*.

A repayment strategy being considered as credible does not remove the consumer's responsibility to ensure it meets its objectives.

4.8A Execution-only sales

The customer's best interests

4.8A.4 G *Firms* are reminded that MCOB 2.5A.1R (The customer's best interests) applies in all cases, including in relation to *execution-only sales*.

4.8A.5 R A *firm* must not encourage a *customer* to opt out of receiving *advice* on *regulated mortgage contracts* from, or reject *advice* given by, it or any *associate*.

If a firm offers both an advised and an execution only service and discloses to the customer that this is the case, is this seen as an encouragement? What if the firm advertises both its advised and execution only service? We consider this to be "encouragement".

Managing execution-only sales

4.8A.14 R A *firm* which intends to transact *execution-only sales* in *regulated mortgage contracts* must have in place and operate in accordance with a clearly defined policy which:

(1) sets out the amount of business the *firm* reasonably expects to transact by way of *execution-only sales*; and

(2) sets out its processes and procedures for ensuring compliance with the *rules* in *MCOB 4.8A*; in particular:

(a) how it will ensure in every case that, before proceeding with an *execution-only sale* it has obtained (where required) a voluntary and informed positive election from the *customer* in order to comply with *MCOB 4.8A9R(3)*;

(b) how it will ensure in every case that it acts in compliance with *MCOB 2.5A.1 R* and *MCOB 4.8A.4 R* (The customer's best interests), including not encouraging a *customer* to enter into a *regulated mortgage contract* as an *execution-only sale*; and

(c) how it will identify whether a *customer* meets the definition of *high net worth customer* or *professional customer*, if it will offer *execution-only sales* to those *customers*; and

(3) includes the arrangements for monitoring and auditing compliance with the policy, processes and procedures.

We consider that there may be circumstances where an intermediary might provide advice on a direct deal, but the consumer might then transact with the lender on an execution only basis. The sale would be advised but would then show on the lender's records as execution-only. This has record keeping issues for the industry and need to be considered where the lender might take subsequent activity relating to the mortgage. This links to our concerns where lenders are asking to make changes on a "transactional" basis, which we consider would rightly be "advice" under these proposals.

Chapter 4

Q21: What is your view on our approach to assessing affordability for interest-only mortgages?

We agree that a repayment mortgage is generally the logical starting point for most consumers. Those that do wish to opt for an interest-only approach should be able to demonstrate a credible repayment strategy.

We are concerned about the term 'speculative' repayment strategy in the context that it is used by FSA. All forms of repayment strategy have some level of speculation.

We understand from our presence at FSA's MMR Roadshow in London that the term speculative is only meant to apply to inheritance and property price increase not to equity investments. This needs to be clarified in the policy intention and in the rules.

We have seen recent evidence of lenders already applying changes to their criteria to change the types of repayment strategies they will accept.

The rules will need to allow consumers who are experiencing financial difficulties to make necessary changes to their repayment method before going into arrears. An outcome where it is more advantageous to go into arrears, to benefit from the lender's forbearance policy, rather than to

proactively try to address any affordability issues before a problem is crystallised, would be failure of the MMR.

Furthermore, FSA interest-only proposals could create the scenario that a consumer would find it much easier to obtain a lifetime mortgage, rather than an interest only mortgage, at a substantially lower rate.

We strongly agree that any changes to the interest-only rules should not be applied retrospectively. Our support of these interest-only proposals is reliant on them not being applied retrospectively.

Q22: Do you agree that we should apply a consistent approach to regulating interest-only across the board and that we should not adapt our approach according to different consumer types?

The rules should be consistent but in doing so they should not restrict certain groups of consumers from being able to obtain interest-only products.

Q23: Do you agree with our non-prescriptive approach to repayment strategies, or do you have any comments on this approach?

We support the flexibility that these proposals give. Lenders should be able to set their own risk tolerances. However, we are concerned that FSA needs to clarify its views on speculative repayment strategy.

Q24: Do you agree that lenders should be free to set their own appropriate controls around repayment strategies?

See question 23

Q25: What is your view of our proposals for lenders' interest-only policies?

See question 21

Q26: What are your views on our approach to requiring lenders to assess the repayment strategy prior to entering into the mortgage?

We agree that the repayment strategy should be stated before the mortgage is entered into. FSA rules need to be clear that the lender/intermediary is not guaranteeing the repayment strategy by stating that it meets the lenders' interest-only lending policy for repayment strategies. FSA needs to clarify how accountable the lender will be if the repayment strategy does not repay the debt in full at the end of the term.

Ultimately the responsibility for the repayment strategy must always remain with the consumer. Any assessment of the repayment strategy either at the initial assessment, or at a periodic check, whether instigated by the lender or the consumer, does not transfer the responsibility from the consumer to the lender.

In identifying the repayment strategy it is important to remember that in reality some consumers will often use more than one repayment strategy to repay their interest only mortgage. To have more than one repayment route would seem sensible and many consumers will have this in place.

Q27: What is your view of our proposals for the ongoing management of interest-only loans? Do you foresee any practical issues?

We agree that there should not be a set point at which periodic checks takes place, other than that they should take place whilst there is still sufficient time to address any adverse outcomes resulting from such checks. FSA must ensure that lenders' interest-only policies are effective

Q28: Do you have any comments on the proposed changes to the glossary term, or the consequential changes?

The change to the glossary terms provides greater clarity as to how the interest-only mortgage could be repaid.

The term 'repayment vehicle' is limited to only including investment based products. Changing the glossary term to 'repayment strategy' incorporates the wide scope of methods that consumers use to repay their mortgage. We are supportive of this change.

Q29: Do you have any comments on the draft interest-only rules set out in the draft *Mortgage Market Review (Conduct of Business) Instrument 2012* at Appendix 1? Do you think the rules reflect the stated policy intention?

No definition is given to the type/level of board that signs off the lender's interest only lending policy. There is no 'board' definition in the glossary of terms in FSA's handbook.

Is FSA intending this to be conducted at a a risk level or non-exec level? Furthermore, for many lenders there will be a consideration of whether this needs to be at a UK, European or global group level?

FSA's handbook Glossary does provide the term 'governing body' which it defines as 'the board of directors, committee of management or other governing body of a firm or recognised body, including, in relation to a sole trader, the sole trader'. This may be a more appropriate term to be applied in the draft rules.

Chapter 5

Q30: Do you have any comments on our proposed approach to intermediaries' role in assessing affordability?

Although the regulatory responsibility will be with the lender, the intermediary will still want to work to ensure, as far as they are able to do so, that the

consumer will meet the requirements of the lender. In reality it will have little impact on the way intermediaries provide advice to consumers.

Q31: (i) Do you have any comments on our proposed approach which allows high net worth consumers and mortgage professionals to opt-out of receiving advice and purchase on an execution-only basis?

We support FSA recognition that not all consumers are the same and that some may favour the ability to opt-out of the new proposals in light of their circumstances.

The justification for applying these exemptions to high-net worth consumers and mortgage professionals is logical. Although exemptions may need to be applied to certain parts of the proposals such as the way a high-net worth consumer's income is considered.

The primary consideration will need to be whether lenders will want to build such models into their business. If mainstream lenders find it too onerous to build such models into their business, then it might be more appropriate to allow those private banks that operate in this area to obtain (or continue to obtain) individual waivers. We do acknowledge that the process for obtaining waivers can be arduous and the 12 monthly renewal requirements is not conducive for many established businesses. However, it must be questioned whether a revision to MCOB is the most appropriate place to address this if it only ends up relating to a small number of niche lenders.

Consideration must also be given to the how the final version of CARRPD will look. Whilst the final CARRPD has not been set, other European financial services directives such a MiFID has already included these types of exemptions within their structures. The recast of MiFID seems set to retain these exemptions and we would expect CARRPD fall in line with MiFID on these issues.

(ii) Do you have any comments on our proposed definition of a 'mortgage professional'? (A question about the definition of a high net worth consumer is at the end of paragraph 10.83 in Chapter 10.)

The issue of this exemption is not so much about the definition but about how lenders will actually apply this exemption. Would both parties to the mortgage need to be mortgage professionals?

Whilst the ability to offer such an exemption may be written into the rules we are concerned how lenders will be able to build the professional exemption into their systems.

(iii) Is there anything we can do to mitigate the risk of intermediaries using these exceptions to circumvent the rules?

No

(iv) Are there any other consumer types you think should be able to purchase on an execution-only basis in an interactive sale?

We do not believe that these exemptions should be extended. They should be left in line with the current European thinking.

Q32: Do you have any comments on our proposed approach which allows consumers to opt-out of advice when purchasing products online or by post and allows them to purchase on an execution-only basis?

Consumers must be able to purchase on an execution-only basis via the internet or by post if they wish to do so. But FSA supervision will need to ensure that such transactions do not end up resulting in interaction, which then turns this into an advised sale.

We would envisage that such transactions would not be the normal consumer route and that advice would still be the default position for lenders offering such services. Therefore, the number of sales proceeding on this basis should be low and FSA should monitor them closely to see that they do not substantially increase over time, as a means of circumventing the rules.

FSA will need to be clear about the areas which incentivise a consumer to pursue an execution only route. Does an adviser informing a consumer that they offer an execution only service constitute encouraging a consumer to opt out of advice? Informing a consumer of the scope of services offered is an important disclosure provision. Furthermore, will lenders be able to offer preferential rates on internet-only (and therefore execution only) deals, even if they also offered an advised route. Surely there can be no greater encouragement for a consumer to forgo the appropriate advised process and opt for the execution only route than the incentive of a perceived lower rate, based on the limited information presented to them on a single lender's website.

Q33: (i) We are proposing that consumers who are vulnerable (i.e. equity release, Home Purchase Plan, Sale and Rent Back or right-to-buy consumers and those who are consolidating debt) should always be advised and therefore will not be able to purchase their mortgage through a non-interactive process. Do you have any comments on this approach?

We support these vulnerable consumer groups receiving mandatory advice. It will provide the additional consumer protections that will drive good consumer outcomes.

However FSA may wish to consider that with the introduction of a broadly advised regime, the customer best interest rule and enhanced affordability provisions, there is no need to adopt such a rigorous approach.

(ii) What are your views on our proposal to allow high net worth consumers and mortgage professionals to opt-out of receiving advice irrespective of whether they are considered to be vulnerable?

We would envisage that the number of consumers falling in to this category would be limited. However, for the same justification as applied to the high-net worth and mortgage professional for non-vulnerable consumers, these exemptions should still be provided. The only exception being Sale and Rent Back transaction which should always be fully advised.

(iii) Are there any other consumer types you think should always receive advice?

Those consumers who are using the transitional arrangement should only be able to proceed on an advised basis.

Some have called for first time buyers to be included and there is certainly some justification for doing this. However, FTBs vary considerably in their circumstances and overall we agree with FSA's position not to include them within the vulnerable consumer classification.

Q34: Do you agree that, except in the case of Sale and Rent Back, we should allow consumers to reject advice and proceed on an execution-only basis?

We agree that these consumers should be able to reject the advice and proceed on an execution only basis if they are able to demonstrate that they understand the implications / consequences of proceeding down this route (e.g. future complaints), and understand enough about the product(s) being arranged from them and key differences between what was recommended and what they wish to proceed with. The adviser should demonstrate that they have provided sufficient information for the customer to make an informed decision in line with FSA's proposals. However, in reality the product should not be too far away from the consumer's actual needs and circumstances. If such a point in the discussions has been reached it may be an issue that the consumer has not made clear to their adviser. It is more likely that the fact find may need to be revisited to discuss the issue in more detail to ensure that the advice provided is aligned correctly clients' needs and circumstances.

Q35: (i) We are proposing that intermediaries monitor their execution-only business. Do you have any comments on our proposed approach to monitoring?

It is not only intermediaries which will need to be monitored. All sellers should monitor their execution only sales, whether they are intermediaries or sales via lender's branches or call centres.

(ii) Are there any other steps we should take to ensure that consumers are protected when purchasing on a non-interactive basis, e.g. should we place any other limitations on the types of consumers who are able to purchase online?

The number of consumers who transact on this route should be limited. FSA should monitor the number of transactions via this route to ensure that they are not excessive.

Q36: Do you agree that we should be specific about the appropriate method of disclosing service fees that are not simple flat fees?

The proposals on this issue are clear and give clarity to intermediaries as to what is required of them.

Q37: Do you have any comments about our revised approach to the requirements for the messages on product range and remuneration to be given 'clearly and prominently'?

Service offering, product range and remuneration remain the most important messages to provide to the consumer. We remain concerned about how oral disclosure is adequately recorded, in particular for small firms when disclosure takes place on a face to face basis.

Q38: Do you consider that the combined IDD template remains useful with respect to mortgage service disclosure?

There is no IDD requirement in ICOBS. If MMR moves to no IDD requirement for MCOB then it would only really be relevant for mortgage sales that also involve investment advice, such as an interest-only mortgage with an investment as the repayment strategy.

It would seem unlikely that the advisor would know this at the start of the sale. However, we would not want to remove the option for firms to continue to use the combined IDD if it is the route they want to go down.

Q39: Do you agree that we should not apply the 'independent' and 'restricted' labels to the mortgage market, but instead require intermediaries to explain to the consumer in clear and straight forward terms any limitations to their service?

We would agree that the RDR labels of 'independent' and 'restrictive' are not the most appropriate fit for the mortgage market.

The ability to allow intermediaries to describe to consumers their own service is a better approach. We welcome the guidance on this issue that FSA has provided in draft rules. In particular, the example scope of service descriptions in 4.4A.6 G. We would support the inclusion of these within the final rules.

Q40: Do you have any views about our updated proposals for product disclosure?

We welcome the reduction in the number of trigger points for issuing KFIs. FSA research has shown that consumers do not use KFIs to shop around,

instead they are used as a record of the product purchased. FSA's proposed rules now take account of this.

Q41: Do you have any comments on the draft rules on distribution and disclosure as set out in the draft *Mortgage Market Review (Conduct of Business) Instrument 2012* at Appendix 1?

11.6.3 R When assessing for the purposes of *MCOB* 11.6.2R whether a *customer* will be able to pay the sums due, a *firm*:

- (1) must not base its assessment of affordability on the equity in the property which is used as security under the *regulated mortgage contract* or is subject to the *home purchase plan*, or take account of an expected increase in property prices;
- (2) must take full account of:
 - (a) the income of the *customer*, net of income tax and national insurance; and, as a minimum
 - (b) (i) the *customer's* committed expenditure; and
(ii) the basic essential expenditure and basic quality-of living costs of the *customer's* household;
- (3) (if it is a *mortgage lender*) must assess affordability on the basis of both repayment of capital and payment of interest over the term, except where lending under an *interest-only mortgage* in accordance with *MCOB* 11.6.24R(1); and
- (4) (if it is a *mortgage lender*) must take account of the impact of likely future interest rate increases on affordability, as set out in *MCOB* 11.6.16R.

Flexibility must be given to the variations in basic essential expenditure and basic quality of living costs. There should not be a one size fits all approach.

Chapter 6

Q42: Do you have any comments on the proposed policy approach on the calculation of payment shortfall charges?

No comment

Q43: Do you have any comments on the proposed policy approach on direct debit payments?

No comment.

Q44: Do you have any comments on the proposal to extend the application of *MCOB* 12.4 and 13.3 rules to include payment shortfalls?

No comment

Q45: Do you have any comments on the proposal to replace *MCOB* 12.4.1 R (2) with a rule permitting firms to remove concessionary rates

where there is a material breach of contract unrelated to payment shortfall?

No comment

Q46: Do you have any comments on the draft rules on arrears management as set out in the draft *Mortgage Market Review (Conduct of Business) Instrument 2012* at Appendix 1?

Chapter 7

No questions

Chapter 8

Q47: Do you agree that the new prudential requirements are unsuited to meeting the objectives of the MMR, specifically deterring high-risk lending?

No comment

Chapter 9

Q48: Do you have any comments on the proposed risk-based capital requirement?

No comment

Q49: Do you have any comments on the proposed restriction in the eligible capital calculation?

No comment

Q50: Do you have any comments on this proposed liquidity regime?

No comment

Q51: Do you have any comments on the proposed scope and application of the regime?

No comment

Q52: Do you have any comments on the draft rules set out in the draft *Prudential Sourcebook for Mortgage and Home Finance Firms, and Insurance Intermediaries (Non-Bank Lenders) Instrument 2012* at Appendix 1? Do you think the rules reflect the stated policy intention?

No comment

Chapter 10

Q53: Do you have any comments on our views, summarised in the table at the end of this chapter, about the MMR proposals which are either not applicable or where a straight read-across to the equity release market is appropriate?

No comment

Q54: What are your views on our proposal to treat the equity release market as a single market for regulatory purposes?

As stated in our previous submission, we support the move to consider equity release as a single relevant market.

Q55: Do you have any comments on the tailoring we propose in relation to execution-only sales following rejected advice and scope of service?

We agree with the execution only product information required for both lifetime and home reversion plans.

Q56: Is any other tailoring required for the equity release market? If yes, please explain.

The majority of Equity Release plans involve the roll up of interest. However, there is one current plan which allows the customer to make monthly interest payments. In such circumstances, if the customer fails to make the monthly interest payments, the plan automatically reverts to a roll up of interest scheme. One of the reasons customers opt for this type of interest only Equity Release plan compared to a traditional interest only mortgage, is because they are aware that they have the safeguard of the plan reverting to a roll up of interest in the event of any payment difficulties. Given this, in such circumstances, we believe Equity Release plans should be exempt from the income, expenditure and affordability requirements given that the terms and conditions of the plan confirm the automatic transfer of the plan to roll-up of interest basis in the event of default on the monthly interest payments. Therefore, there is no risk of any customer detriment.

Q57: Overall, do you have any other comments on our proposed read-across of the MMR to the equity release market?

No comment

Q58: Do you have any comments on our views, summarised in the table at the end of this chapter, about those mainstream MMR proposals which are either not applicable or where a straight read-across to the Home Purchase Plan market is appropriate?

No Comment

Q59 Do you have any comments on the tailoring we propose in relation to execution-only Home Purchase Plan sales following rejected advice and enhancing sales standards?

No Comment

Q60: Is any other tailoring required for the Home Purchase Plan market? If yes, please explain.

No Comment

Q61: Overall, do you have any other comments on our proposed read-across of the MMR to the Home Purchase Plan market?

No Comment

Q62: Do you have any comments on our views, summarised in the table at the end of this chapter, about those mainstream MMR proposals which are either not applicable or where a straight read-across to the Sale and Rent Back market is appropriate?

We support the view that Sales and Rent Back should always be transacted on an advised basis.

Q63: Do you have any comments on the tailoring we propose in relation to not allowing Sale and Rent Back consumers to reject advice?

See question 62

Q64: Is any other tailoring required for the Sale and Rent Back market? If yes, please explain.

No, there should be no further tailoring for this product.

Q65: Overall, do you have any other comments on our proposed read-across of the MMR to the Sale and Rent Back market?

We are concerned that the sale and rent back market has recently been consulted on by FSA and then more recently closed altogether. We do not believe that further tailoring should be applied to this product which could water down the provisions made in those consultations.

Q66: Do you have any comments on our proposal to define a bridging loan as a regulated mortgage contract with a term of 12 months or less?

We support this definition as FSA proposes it to be applied. This will provide clarity on this particular market/product.

Q67: Do you have any comments on how the affordability proposals should be applied to consumers taking out bridging finance?

We support the proposals on how affordability is assessed where a monthly payment is and where it is not required.

Q68: Do you have any comments on our proposed read-across of our interest-only proposals to bridging finance?

What constitutes a creditable repayment strategy for bridging finance will be different to that of a residential interest only mortgage. However, we agree that it is important that the borrower has an exit strategy when they take out bridging finance.

Q69: Do you have any comments on our proposal that lenders consider the repayment or exit strategy of the borrower, and have a clear lending policy that reflects this?

Bridging finance is generally used as a flexible form of borrowing. The considerations around acceptable repayment strategies will need to reflect this.

Q70: Do you have any comments on our proposals about extending bridging finance loans?

It would make sense to reassess the repayment strategy at the time of extensions. However, it is likely that the planned repayment method remains unchanged and it is simply the time scales that have shifted.

Q71: Are there any other factors that firms should consider in order to determine that a bridging loan is appropriate?

No

Q72: Do you have any comments on our proposal which requires that intermediaries who only offer bridging loans should describe the restriction on their service to the consumer?

Given the relevant market we agree with FSA proposals that such a restriction must be disclosed to the consumer. A mortgage adviser who can consider both residential and bridging loans will provide a very different scope of advice to one that can only consider bridging loans.

Q73: Do you have any comments on the proposed prudential regime for bridging lenders?

No comment

Q74: Do you agree with our views, summarised in the table at the end of this chapter, about the MMR proposals which are either not applicable or where a straight read-across to the bridging finance market is appropriate?

Yes

Q75: In addition to the proposed tailoring set out above, is any other tailoring required for the bridging finance market? If yes, please explain.

No

Q76: Overall, do you have any other comments on our proposed read-across of the MMR to the bridging finance market?

No comment

Q77: What are your views on our approach to high net worth consumers? Should we adopt a more freemarket approach, recognising that for some consumers, regulation is not needed to protect them from the decisions they make?

These consumers should have the opportunity to opt-out of some proposals. The opt-out should be voluntary rather than a mandatory exclusion of high net worth consumers. This would allow those HNW consumers who still want to go through the full process to do so.

Q78: Would an elective approach similar to that adopted in the investment market be appropriate?

Yes it should be based on the MiFID provisions, which have then been transposed through COBS. FSA must also be mindful of how such exclusions will be dealt with under CARRPD.

Q79: Would it be appropriate for all mortgage rules to be forgone?

The definition of high-net worth is set at a high level. However, there is a clear relationship between the level at which the HNW definition is set and the level of rules which are forgone.

HNW consumers are different from mainstream borrowers and the MMR proposals are right to acknowledge this. Providing that sufficient safeguards are in place, such as consumers having to proactively opt-out and that there is independent verification of their HNW status, eg via an accountant, then they should forego mortgage conduct rules.

HNW consumers should be made aware of the protections they are giving up by opting to use the HNW exemptions.

The key benefit we would see would be greater flexibility around the affordability assessment. Where income may come from more complex sources such as family trust and a robust assessment of expenditure is less relevant due to the income levels involved.

Q80: Would it be appropriate for all regulatory protections for high net worth to be forgone or should some, such as redress, for example, be retained?

If opting out of the main stream process resulted in a loss of some FOS rights this would be less of a concern to a HNW consumer than to a non-HNW consumer. This is because HNW consumers are much more likely to have sufficient financial resources (due to the definition) to pursue any grievance on a legal basis as required.

There is also, generally, lower redress considerations for mortgage transactions than for those of investments. The nature of the mortgage transaction places a greater degree of risk on the lender, than the borrower. Those lenders opting to operate a HNW exemptions will need to ensure that they have sufficient systems and controls in place manage their own risks.

Q81: What are your views on defining high net worth consumers – what do you consider the appropriate figures for income and assets?

We agree with the definition provided by the FSA. The proposed definition will ensure that anyone wishing to opt for this exemption will be genuinely HNW. However FSA may also want to consider whether the percentage of borrowing should also form part of the consideration to ensure that the HNW consumer has sufficient funds in the transaction, such as 60% LTV or a minimum, such as £500,000 or a sum at which a suitable property could be financed under the proposals.

FSA must also give consideration any European definition that results from CARRPD.

However, the alternative option may be for FSA to apply waivers to lenders who are prepared to operate in the HNW space rather than applying regulation through MMR. This may be a more tailored option considering the division between lenders who may or may not want to operate in this space.

Q82: Do you agree that it is appropriate to extend the definition to include high net worth consumers acting as guarantors?

We agree with FSA's justification for including guarantors within the HNW definition.

Q83: Do you have any comments on how the affordability proposals should be applied to high net worth consumers?

We support the proposals on how affordability is assessed where a monthly payment is and where it is not required.

HNW consumers will obtain income from a variety of sources which may not be considered as mainstream. The MMR proposals need to account for flexibility for these types of income in its HMW proposals.

Flexibility should also be provided based on the level of mortgage payment relative to their income streams and supporting assets in the background.

Q84: Do you have any comments on our proposal to extend the tailored disclosure rules to high net worth consumers?

We would support the proposed extension.

Most intermediaries would expect 20% - 30% of mortgage transactions to be interest-only sales, depending on the geographical region. There are also high levels of interest-only mortgages as you move up the wealth curve. FSA should not see interest-only as a niche product, in certain markets.

Q85: Do you think that to achieve this, an elective approach similar to that adopted in the investment market would be appropriate?

Yes, see question 78.

Q86: Do you agree with our views summarised in the table at the end of this chapter about the MMR proposals which are either not applicable or where a straight read-across to high net worth lending is appropriate?

Yes

Q87: In addition to the proposed tailoring set out above, is any other tailoring required for high net worth lending? If yes, please explain.

No comment

Q88: Overall, do you have any other comments on our proposed read-across of the MMR to high net worth lending?

No comment

Q89: What are your views on our approach to business lending? Should we adopt a similar approach to that proposed for high net worth consumers, recognising that for some consumers, regulation is not needed to protect them from the decisions they make?

No comment

Q90: How would we draw a line between those business borrowers able to take the risk and those who are not?

No comment

Q91: How would we prevent this proposal from being exploited as a means of circumventing our affordability proposals?

No comment

Q92: Would it be appropriate for all mortgage rules to be forgone or should some, for example the arrears rules, be retained?

No comment

Q93: Do you have any comments on how the affordability proposals should be applied to business borrowers?

No comment

Q94: Do you have any comments on the proposed approach to professional standards in business lending?

Q95: Do you agree with our views summarised in the table at the end of this chapter about the MMR proposals which are either not applicable or where a straight read-across to business lending is appropriate?

No comment

Q96: In addition to the proposed tailoring set out above, is any other tailoring required for business lending? If yes, please explain.

No comment

Q97: Overall, do you have any other comments on our proposed read-across of the MMR to business lending?

No comment

Q98: Do you have any comments on the draft rules specific to niche mortgage markets in the draft *Mortgage Market Review (Conduct of Business) Instrument 2012* at Appendix 1? Do you think the rules reflect the stated policy intention?

No comment

Annex 1 CBA

Q99: Do you have any comments on our estimates for the impacts of the affordability assessment? Do you have any data and/or analyses that could be informative about these impacts?

No comment

Q100: Do you have any comments on our estimates for the impacts of the interest rate stress test? Do you have any data and/or analyses that could be informative about these impacts?

No comment

Q101: Do you have any comments on our estimates for the impacts of the interest-only proposals? Do you have any data and/or analyses that could be informative about these impacts?

No comment

Q102: Do you have any comments on our estimates of the combined impacts of the responsible lending requirements? Do you have any data and/or analyses that could be informative about these impacts?

No comment

Q103: Do you have any comments on our estimates for the lending impacts of the responsible lending requirements? Do you have any data and/or analyses that could be informative towards estimating these impacts?

No comment

Q104: Do you have any views on whether this balance between winners and losers is acceptable, given the importance of the protection obtained by the winners?

The level of consolidation between banking groups and lenders that would not be acceptable under normal market conditions needs to be recognised. To not do so risks ignoring important competition issues could materialise as a result of the changes in MMR. In particular, the ability for these banking groups to unfairly use their customers' current account information in the affordability assessment. Also the Rules could as they stand give lenders the ability to incentivise consumers to self select lower priced execution only mortgage products online, which could be an unintended consequence of MMR's drive towards advice.

Annex 2 EIA

Q105: Do you have any comments on the age-related issues discussed above?

The impact of the proposals on those consumers that approaches retirement age should not be underestimated. Extending the term of the mortgage into a consumers retirement may be in the best interest of the consumers. This is particularly with the abolition of normal retirement ages, and the arrival of portfolio careers in later life.

It is essential to not ignore what those consumers who pre-MMR would have obtained a mortgage into their retirement will do. It would seem likely that FSA's proposals could push more people towards opting for a lifetime mortgage. This will generally be a more expensive route for the consumer. Lenders should take account of consumers anticipated retirement ages, to date one sized fits all thinking has prevailed. In the world moving forwards consumers will be in far more control themselves about when they retire and the Rules should recognise this fact.

Q106: Are there any other age-related impacts from our proposals not highlighted above? If yes, please provide details.

See question 105.

Further consideration needs to be given to the alternative products or solutions that the consumers affected by the restriction of products, whether directly to indirectly as a result of their age will have.

Consumers will seek alternative products. The additional costs that these will inevitably be higher for consumers, in particular in the use of equity release.

Q107: Do you have any comments on the disability-related issues discussed above?

No comment

Q108: Are there any other disability-related impacts from our proposals not highlighted above? If yes, please provide details.

No comment

Q109: Do you have any comments on the gender-related issue discussed above?

No comment

Q110: Are there any other gender-related impacts from our proposals not highlighted above? If yes, please provide details.

No Comment

Q111: Do you have any comments on the pregnancy and maternity-related issue discussed above?

The additional requirements for assessing future changes in circumstance could push advisers to further question whether applicants may be planning a family, in the foreseeable future. Such a question could be seen as leading the witness. Careful consideration needs to be given by FSA as to how these proposals fit within gender discrimination laws given that the answers given could potentially impact on whether or not a mortgage is obtainable

Q112: Are there any other pregnancy and maternity-related impacts from our proposals not highlighted above? If yes please provide details

No Comment

Q113: Are there any race-related impacts from our proposals that we should consider? If yes, please provide details.

No comment

Q114: Do you have any comments on the religion-related issues discussed above?

No comment

Q115: Are there any other religion-related impacts from our proposals not highlighted above? If yes, please provide details.

No comment

Q116: Are there any sexual orientation-related impacts from our proposals that we should consider? If yes, please provide details.

No comment

Q117: Are there any transgender-related impacts from our proposals that we should consider? If yes, please provide details.

No comment

Q118: Do you have access to, or know of, any statistics regarding the mortgage needs and habits of groups with protected characteristics that could help us with our analysis? If yes, please provide details.

No comment

ENDS